SOME ASPECTS
OF
INDIAN ECONOMIC DEVELOPMENT

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(a study of the leading problems of Indian Economics)

VOL. II

BY

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PREFACE

The present volume continues and completes the study begun in volume one. Though each volume is self-contained and is complete by itself, they are intended to be complementary, and, hence supplement each other. For the convenience of the reader, appropriate references to Volume I have been indicated.

The approach of Volume II is similar to that of Volume I. I have laid stress on the regional aspects of development wherever necessary. In many topics, however, regional or statewise analysis is unnecessary, as, for example, in problems connected with Currency, Banking, Foreign Trade etc.

It has been my endeavour to stimulate thinking and promote appreciation rather than merely to supply factual information. As students of planning, and living in an age of planning, most of us are obviously "day-dreamers". I am, probably, no exception to this general rule ; but, I have tried to be realistic and objective as far as possible.

I need hardly add that the views expressed are entirely personal and do not reflect the views of any Department, Organisation or Institution.

New Delhi.
25th July. 1962

S. K. Bose

PREFACE TO VOL. I

The book is intended for the intellectual elite of the country,—the University students, the teacher, the men of public affairs and the citizen interested in the problems of our country. India has gone through vast changes during a decade of planning and it is necessary to take stock of the achievements (and failures) in different fields of her economic life. It is hoped that the book will enable an appraisal of our various problems.

For the convenience of the reader, particularly the student-reader, I have adopted the rather unconventional method of paragraph and sub-paragraph numbering; this is intended to indicate that each paragraph deals with an important connected issue while the sub-paragraphs demarcate its different facets. For instance, Chapter XI deals with Planning in India, Para 4 of it is concerned with Resources for the Plan; all sub-paras under Para 4 are discussions of resources, and, sub-para 4·4, for example, examines a specific item of these resources, namely, deficit financing with sub-paras 4·4·1 or 4·4·3 considering some special aspect of it. I hope the reader will find this arrangement helpful for methodical study, especially as I have often used the word "note" in particular paragraphs to indicate that more is stated elsewhere.

A fairly long period of service as a teacher and as a civil servant enabled me to come in close contact with people who can think for themselves. I have acquired a high regard for the intellectual capabilities of our people. I found them impatient with longwinded verbosity and sceptical of unreasoned assertions that sounded like Commandments. I have, therefore, endeavoured to be brief, bordering perhaps on terseness, and have tried to give detailed basic information on the problems analysed. As regards the statistical data, I have drawn heavily on 'official' statistics, that is, statistics published by departments of Central and State Governments, and, the information made available by the National Sample Survey. The N.S.S. data, it may be pointed out, is often subject to margins of error and should, therefore, be used with caution; its limitations are many and those who are acquainted with sampling techniques and the nature of the sample survey organisation in India have found it full of pitfalls. I have

also used relevant data made available by research organisations and non-official agencies, as I believe that the nature and appropriateness of a data is more important than its source.

I owe a deep debt of gratitude to my *guru* Mr. K. C. Nag, from whom I not only learnt the elements of economics but also the importance and value of intellectural integrity. I must also express my gratitude to Dr. V.K.R.V. Rao from whom I have always received affectionate guidance and kind help, both while working as one of his Junior Colleagues in the University of Delhi, and also later. In fact, without my continued contact with them and with my erstwhile colleagues I could hardly have kept up my interest in a technical subject like economics.

I must thank my wife, Namita, who by running the household smoothly despite rising prices, a fixed income and a husband indifferent to domestic problems made possible the undertaking of such a venture. She also helped me with the reading of proofs and the preparation of the index. My thanks are also due to my son, Gautam Bose, now an Economics Honours student in St. Stephen's College, my own *alma mater*, who gave me the first draft of the list of topics to be covered and who acted as my "representative" reader as I wrote each chapter. Mr. R. M. Shahani and Mr. M. C. Gupta of Ranjit Printers and Publishers have borne patiently the idiosyncracies of an author, and, I am grateful to them for having brought out the book in a remarkably short period.

Finally, I should like to emphasise that the views expressed are purely personal and do not, in any way, reflect the views of any Department, Organisation or Institution. I might add that I have been emboldened to express views on the economic problems of our country by what our beloved Prime Minister stated in the course of his speech in the Lok Sabha on August 22, 1960 :—

"I should like to repeat that the Planning Commission or the Government of India do not regard themselves as being in possession of the ultimate wisdom. They invite friendly consideration, and even unfriendly consideration, provided it is intelligent..........."

I can only hope that the intelligent reader, even when differing from my views, would, at least, regard them as intelligent.

NEW DELHI,
January 26, 1962. *S. K. Bose*

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THE STATE AND SOCIAL WELFARE

1. The Welfare State in India

1·1 As the midnight bell tolled on August 14, 1947, leaders of the nation took over the administration of a vast country. It was a country starved of the many necessities of life; it was a country that had a miserably low level of education; it was a country with widespread poverty[1]. It was, however, also a country with a people that had shown through centuries an indomi—table will. The Government of the country was entrusted with the responsibility of revitalizing an economy that had been static for generations. The State had to open a new and better way of life for the people.

1·2 The people of India gave themselves a Constitution that made the country a Sovereign Democratic Republic in which a duty was imposed on the State to raise 'the standard of living of its people'. The concept of the level of living for a nation is not merely the concept of enhancing the income-earning capacity of the individual, it also involves the State providing the many essential amenities of life which are a part of the inherent right of the people. These rights are :—

(a) the right to education,

(b) the right to an improvement in public health,

(c) the right to public assistance in cases of—

(i) unemployment,

(ii) old age,

(iii) sickness and disablement,

(iv) undeserved want,

(d) the right to just and humane conditions of work, and

(e) the right to a full enjoyment of leisure and social and cultural opportunities.

The directive principles of the Constitution of India

1. See Vol. I, Ch. I paras 23 to 25.

recognise these rights of the citizen, and, the framers of our Constitution have wisely laid down that these principles are 'fundamental in the governance of the country' and that 'it shall be the duty of the state to apply these principles in making laws'.

1·3 The goal of India is a socialistic pattern of society[2]. We are aiming at a socialist economy that would be "Capable of growing steadily to a level at which the well-being of the mass of the population can be secured......it should provide for the basic necessities, in particular, for food, work, opportunity for education, reasonable conditions of health and sanitation, improvement in conditions of housing and a minimum level of income......"[3] These heavy responsibilities must mean a rising level of welfare expenditure of the Central and State Governments, particularly of latter as the constitutional division of functions and responsibilities imposes on the states the more expanding welfare functions. Further, social welfare expenditure, apart from the directly beneficial effects, also helps to bring about redistribution of income, especially when financed by a progressive tax system.

2. Trends in Social expenditure.

2·1 *The Central Budget.*[4] The primary development expenditure of the Union Government is comparatively low, because most of the expenditure incurred for such purposes by it is through grants—plan and non-plan—to the state. The practice upto 1961-62 was to indicate central grants to states for such terms under the major heads of accounts to which the grants relate and were taken as receipts under the relevant heads by the states. This arrangement had two serious defects *viz.*,

(a) it inflated the receipts of the State Governments under the concerned major head,

(b) it gave a grossly inflated picture of the total expenditure of the Central and State Governments taken together, which was to a great extent illusory for the central grants were not final expenditure but were only transfer of resources from the centre to the states.

From 1961-62, a change in the budgetary practice has been introduced and all the grants to States for the social and Developmental sevices are being shown separately as grants;

2. See Vol. I, Ch. I paras 2·4 to 2·5.
3. Third Five Year Plan p. 10, the level of living and per capita income has been dealt with in Vol. I
4. See Vol. I, Ch. IX paras 1·1 to 3·5.

thus figures for 1961-62 are not straightaway comparable with those for earlier years. However, some idea of the growth of expenditure under these categories may be got from the table given below :

(In Rs. Lakhs)

Item	1951-52	1956-57	1958-59	1960-61 (R.E.)	1960-61 (B.E.)
(1)	(2)	(3)	(4)	(5)	(6)
1. Scientific departments	5,18	11,05	16,44	23,08	31,89
2. Education	4,08	19,44	27,89	44,16	53,67
3. Medical	1,51	2,87	5,64	8,28	8,81
4. Public Health	80	3,35	7,77	10,44	17,22

Since these items are essentially in the state list of functions, except to some extent the first item, there is no reason to expect any substantial growth of expenditure so far as the Union Government is concerned. Further, the plannig process has included these as major items of plan provision and most of the expenditure in recent times has been under the plan. Taking the two most important items, we find the position as follows :—

(Expenditure in Rs. Crores)

Item	First Plan	Second Plan	Third Plan*
Education	149·0	255·8	560·0
Health	97·9	216·3	342·0

2·2 The expansion in both has been very rapid, having grown nearly fourtimes in ten years. Development of important social services are measures for improving the quality of the people and are, both directly and indirectly, measures for securing greater equality of opportunities and raising levels of living through greater social mobility. Social services, it may be emphasised, are vital ingredients in the scheme of economic development and are the foundations on which economic progress rests. It has often been emphasised that men are more important than material so that improvement of the human agent of production should naturally be the prime concern of planned economic development in India. Nearly a quarter of a century ago, a distinguished son of India stated,[5]

* Target.

5. Dr. Meghnad Saha, Presidential address, National Institute of Sciences of India. 1938.

"If we desire to fight successfully the scourge of poverty and want from which 90 percent of our countrymen are suffering, and lay the foundation of a strong and progressive national life, we must make the fullest use of the power which a knowledge of Nature has given us. We must rebuild our economic system by utilizing the resources of our land, harnessing the energy of our rivers, prospecting for the riches hidden under the bowels of the earth, reclaiming deserts and swamps, conquering the barriers of distance and above all, we must mould anew the nature of man in both individual and social aspects, so that a richer, more harmonious and happier race may live in this great and ancient land of ours".

These were not mere idealistic dreams but the wisdom of a visionary, the truth of which it has taken nearly 25 years for us to realise.

3. Education in India

3·1 Education, including literacy and skills, has always, been accepted as an important component of the level of living, and, various indicators are adopted for showing how far it has made its appropriate contribution to national welfare.

3·2 The U. N. Committee of experts in their report on measurements of Standards and levels of living listed some indicators[6] and adapting these, one may use the following important ones :—

(i) proportion of children 5—14 years of age attending or enrolled in schools;

(ii) attendence of other age groups *i.e.*, 11—14, and, 14-17, to the total in each group;

(iii) Pupils per teacher in—
  (a) primary schools,
  (b) Secondary education,
  (c) University education;

(iv) Number of Educational Institutes of different categories,

(v) expenditure on education.

3 3 Article 41 of the Constitution of India enjoins the directive principle that "the State shall, within the limits of its economic capacity and development, make effective provision for securing the right to......education......"; ensuring of which is the first step towards achieving a state policy directed towards securing "that childhood and youth are protected against exploitation and against moral and material abandon-

6. See Vol. I, Ch. III, para 2.

ment". Education, including Universities, is item 11 of List II (statement first) of the Seventh schedule of The Constitution of India, and, is essentially a responsibility of State Govts. A fundamental Right guaranteed under Article 29 (1) is "Any section of the Citizens residing in the territory of India or any part thereof having a district language, script or culture of its own shall have the right to conserve the same", while Article 30 (1) guarantees the right to all minorities to "establish and administer educational institutions of their choice". State Governments obviously must undertake adequate expenditure on education if its appropriate development is to be ensured. To the extent expenditure on education is a part of the normal expenditure of the States and their commitments in respect of the plan expenditure on revenue account, its undertaking is not merely a necessary expenditure but of primary importance the emphasis on which should steadily become greater.

3·4 There has been a steady increase in the facilities of schooling for children in different age groups :—

	% in schools to total in each group			
	1950-51	1955-56	1959-61	1965-66
Age 6-11	43·1	51·0	60·0	80·0
Age 11-14	12·9	16·3	22·6	30·0
Age 14-17	5·4	8·1	12·0	15·0
			(Estimate)	(Target)

(For details, See Vol. I, Ch. I, table 18.)

3·5 So far as university education is concerned, growth in absolute numbers of enrolment is a better guide, for restriction of the facility of higher education to those likely to derive the highest benefit out of it generally leads to a lack of specific correlation between numbers on roll and total numbers in the age group.

	1950-51	1953-44	1955-56	1958-59	% growth in 1958-59 over 1950-51
Universities (No.)	27	30	32	40	40
Colleges (No.)	498	613	712	869	80
Enrolment (No.—000)	342	471	573	713	100

3·6 But growth in numbers is a quantitative expansion. Generally it is believed that appropriate teacher-pupil ratio is the basic requirement for qualitative appraisal. The position in this respect can be seen from the following table :—

Pupils per Teacher

Items	1950-51	1955-56	1958-59
1. Per-Primary Schools	25	24	27
2. Primary Schools	34	33	34*
3. Secondary Schools	25	20	30
4. Universities	14	15	16

*Relates to 1957-58.
(For details, See Vol. I, Ch. I, Table 19.)

3·7 Development and expansion in the field of education can be judged by analysing the growth of institutions of different categories, and, appears substantial as would be indicated from the following table :—

Index of growth of Educational Institutions in India

Items	(Base 1950-51=100) 1955-56	1958-59
1. Universities	118	143
2. High/Higher Secondary Schools	149	193
3. Middle/Senior basic/ Junior High Schools	160	199*
4. Primary/Junior basic/ Basic Primary Schools	132	142
5. Colleges for General Education	143	180
6. Schools for Special Education	96	97
7. Schools for vocational Training and Technical Education	131	146

*Relates to 1957-58.

3·8 *Basic Education* :—It has been decided to model all elementary schools on the basic pattern. It is hoped that by the end of the second plan about 24% will be on the basic pattern and the process will be carried forward in the Third Plan. Some idea of the progress is indicated below :—

Index of Growth in Basic Education

Items	(Base 1950-51=100) 1955-56	1958-59
Schools	142	192
Enrolment	174	260

3·9 *Technical Education* :—With the growing industrialisation of the country growth of institutions catering to Engineering and Technology are expected to increase steadily. The following table gives some idea of this growth :—

Index of Growth in Education—Engineering and Technology (Base 1950-51=100)

Items	1955-56	1957-58
1. Engineering Colleges	148	181
2. Technology Colleges	117	117
3. Pupils inEngineering Colleges	142	204
4. Pupils in Technology Colleges	218	230
5. Engineering Schools	197	287
6. Technology Schools	131	142*
7. Pupils in Engineering Schools	412	566
8. Pupils in Technology Schools	97	120

*Relates to 1956-57.

3·10 The financial implications of expenditure on education by the Central and State Governments are indicated in the following tables :—

TABLE I

Central and State Governments—Expenditure on Education (In lakhs of Rs.)

	1956-57	1957-58	1958-59	1959-60	1960-61
Centre	19,44	20,98	27,89	37,42	45,35
Total Expenditure	500,52	658,86	706,42	795,35	890,13
% of education to total	3·9	3·2	3·9	4·7	5·1
States	114,37	130,46	147,24	163,41	177,32
Total Expenditure	644,58	689,57	768,40	872,25	949,01
% of education to total	17·7	18·9	19·2	18·7	18·7
Centre's Grant to states for Education	6	4·17	11·89	18·53	27,66

TABLE II

Expenditure on Education—Indian Union

(Rs. lakhs)

Type of Institution	1951-52	1957-58	Increase in 1957-58 over 1951-52 Absolute	Percent
Direct Expenditure				
1. Universities	4,98	9,78	4,80	97
2. Boards of education	78	1,76	98	125
3. Research Institution	64	2,94	2,30	359
4. College for general Education	8,11	14,12	6,01	74
5. Colleges for Professional education	5,22	9,45	4,23	81
6. Secondary Schools	26,15	46,44	20,29	78
7. Middle Schools	8,72	20,69	11,97	137
8. Primary Schools	40,40	66,78	26,38	65
9. Pre-Primary Schools	15	33	18	120
10. Schools for vocational education	6,52	10,19	3,67	56
Total-Direct Expenditure	101,67	182,48	80,81	80
B-Indirect Expenditure	22,89	57,91	35,02	153
GRAND TOTAL	124,56	240,39	115,83	93

3·11 As against the anticipated outlay under the second plan of 273 crores on educational programmes, including those relating to technical education, a provision of 500 crores has been made in the third plan. This includes Rs. 370 crores for general education and Rs. 130 crores for technical education, compared to Rs. 213 crores and Rs. 60 crores respectively in the second plan.

4. Economic development of a country is closely related to the attention given by it to scientific education and research. The economic history of the world is evidence of how industrial production and the consequential rise in the income of the people have been the result of developments in the field of science and technology, for scientific research and increased production from improved technology are closely related. In

fect, rapid industrial development, as was achieved by the U. S. S. R., can be realized only by a close and intimate integration between science and industry.

5. Scientific and Technological Development.

5·1 Advances in science and technology are essential if development programmes in industry and allied fields are to achieve the desired rate of progress. Recognising the need for an appropriate role for science and technology in modern India, the Government of India issued a Statement* on Scientific Policy which indicated the role of science and scientific personnel in the overall development of India. India, with its rapidly developing planned economy, must necessarily promote not only fundamental research in all fields but also intensive scientific approach on the many problems of productivity in agriculture, large and small industries and other facets of economic life, especially in the field of heavy chemicals, metallurgical industries, development of energy, etc.

5·2 The previous two plans provided for surveys and investigations of natural resources. Many specific studies have been undertaken by Governmental and other agencies. But, as the Third Five-Year Plan emphasises :

> "The stage has been reached when as a necessary condition of well-conceived long-term plans, a comprehensive view must be taken of the extent and quality of the information available, the principal gaps which exist and the further steps needed in relation to specific long-range objectives concerning the development of irrigation, power, steel, coal, oil and minerals and land and forest resources and the conservation of natural resources generally."

It is possible to hold the view that :

> "an appropriate machinery for planning co-ordinated studies of natural resources on a continuing basis and reviewing the results obtained from time to time has uses to be devised. This may take the form of a Committee of Direction composed of the technical heads of the various agencies concerned with which a few leading scientists are associated and which is assisted by a highly trained staff."

The Third Five-Year Plan proposes to give increasing support to scientific and technical education with a view to increasing the number of pupils taking science courses from 30 to 40 per cent of the total while the intake capacity of

*See, Third Five Year Plan, p. 617.

engineering colleges and polytechnics is expected to increase from 37,000 at the end of the Second Plan to 52,500 at the end of the Third Plan.

5·3 Some idea of the progress and targets relating to technical education—engineering and technology—can be got from the following table :—

(Nos)	1950-51	1955-56	1960-61 (antici-pated)	1965-66 (targets)	% in-crease in 1960-61 over 1950-51	% in-crease in 1965-66 over 1960-61
Degree level (intake)	4,119	5,888	13,165	18,500*	220	41
Diploma level (intake)	5,903	10,484	24,020	34,000*	307	42
Agriculture degree level (intake)	1,060	1,989	4,500	6,000	325	33
Veterinary degree level (intake)	434	1,269	1,300	1,550	200	19

*excludes facilities provided in part-time courses.

5·4 Any planned use of science and technology for national development must necessarily depend for its success on an adequate increase in the number of scientific and technical personnel. In India, in view of the general level of standards, perhaps it would be not inappropriate to define a "scientist" as a person who possesses at least a master's degree in any of the branches of natural sciences which group may be taken to include Physics, Chemistry, Geology, Botany, Zoology and Mathematics (including Statistics).

Some idea of the outturn of scientists and accumulated totals from Indian Universities may be got from the following table overleaf

Year	No. of degrees awarded. Total	Average per year	Index No. 1910-14 =100	Accumulated total No. (Col. 2)	Percentage Col. (5)
(1)	(2)	(3)	(4)	(5)	(6)
1910-14	385	77	100	385	1.2
1915-19	832	166	216	1,217	3.8
1920-24	917	183	238	2,134	6·7
1925-29	1,923	385	500	4,057	12·7
1930-34	2,784	557	723	6,841	21·5
1935-39	2,938	558	764	9,779	30·7
1940-44	3,378	676	878	13,157	41·3
1945	786	786	1,021	13,943	43·7
1946	824	824	1,070	14,767	46·3
1947	901	901	1,170	15,668	49.2
1948	925		1,200	16,593	52·0
1949	939		1,219	17,532	55·0
1950	1,083		1,406	18,615	58·4
1951	1,444		1,875	20,059	62·9
1952	1,693		2,199	21,752	68·2
1953	2,104		2,732	23,856	74·8
1954	2,432		3,158	26,288	82·5
1955	2,659		3,453	28,947	90·8
1956	2,933		3,809	31,680	100·0

The above table brings out that the achievement in this respect up to 1939 was most disappointing, there was little increase during the war and progress was slow till 1950. The first Five-Year Plan gave a good fillip and the number more than doubled in five years from 1,875 in 1951 to 3,809 in 1956.

Some further analysis of the table may be of interest :

(a) Out of 31,880 scientists turned out between 1910 and 1956, 15,668 had come up to 1947;

(b) The total outturn upto 1947 may be regarded as roughly the same as the master's degree was introduced only in 1909 ;

(c) The post-independence number of 16,218 (1948-1956) was greater than total outturn during the whole period before independence.

The above numbers should not, strictly speaking, be taken to connote effective availability for which allowance by death/transfer to non-scientific employment has to be made ;

but for which appropriate statistical data is difficult to construct.

5.5 An interesting study would be to examine more specifically the enrolment and outturn of degree and diploma-holders in engineering and technology in India for the period 1951-59 for which data is readily available :

Year	Degree In-take	Degree out-turn	Diploma In-take	Diploma out-turn	Total In-take	Total out-turn	Index 1951-52 =100 In-take	Index 1951-52 =100 out-turn
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
1951-52	4,788	2,693	6,216	2,626	11,004	5,319	100	100
1952-53	5,184	2,956	6,499	2,654	11,683	5,610	106	105
1953-54	5,450	2,880	7,213	2,747	12,663	5,627	115	106
1954-55	5,468	3,207	8,313	3,397	13,781	6,604	125	124
1955-56	5,937	4,017	9,397	4,072	15,334	8,089	139	152
1956-57	6,367	4,293	9,899	4,075	16,266	8,368	148	157
1957-58	9,778	4,290	15,995	5,034	25,773	9,324	234	175
1958-59	11,086	4,571	19,932	6,021	31,018	10,592	282	199

(Source—Lok Sabha Question No. Education 21.7 on 10th August 1959)

It would appear that upto the period of the First Five-Year Plan (*i.e.* upto 1955-56) progress was slow, understandably because of the comparatively deficient progress in industrial production during the First Five-Year Plan. However, the Second Five-Year Plan placed greater emphasis on industrial production as also on expanding facilities for technical training. The effect was that enrolment which expanded by only about 25 per cent upto 1954-55,more than doubled by 1958-59. So far as admissions to degree level courses in engineering and technology increased from about 6,000 per year in 1955-56 to 11,000 in 1958-59, and are expected to rise to 13,000 in 1960-61.

5·6 The divergence in the Index at Col. (8) and Col. (9) of Table in para 5·5 is an interesting feature for noting. In one way it is an index of unfructified expenditure ; in another, the cost of ensuring quality.

5·7 While international comparisons are often statistically unsatisfactory, one is tempted in this connection to get some idea, admittedly very rough, of the position in India and some of the other countries :

Engineers per Million Population—Total Available

U.S.A.	3,144
U.S.S.R.	3,605
U.K.	1,539
China	132
India	188

(N.B. The years are not identical but range between 1950 and 1956)

5.8 Expenditure figures are often a good guide to the importance of the role of Government in matters of scientific education and development. Two tables are given below analysing the position in India.

(TABLE I)

Revenue Expenditure on Scientific Research and Cultural Affairs. (Rs. lakhs.)

	1957-58 A/c	1958-59 A/c	1959-60 R.E.	1960-61 B.E.
I. Total Expenditure on Scientific Research and Cultural Affairs.	892·24	1087·20	1522·37	2061·00
II. Grants				
(a) Grants to States.	50·66	128·99	200·00	294·00
(b) Grants to Scientific Institutes.	216·24	233·66	259·21	289·25
(c) Grants for Museums.	1·39	2·67	13·47	27·51
(d) Grants for Cultural activities.	105·60	107·01	305·98	517·77
(e) Grants to the Council of Scientific and Industrial Research.	235·00	209·00	345·00	390·00
(f) Grants to Regional languages:				
(1) Grants to States	—	—	—	7·40
(2) Grants to others	—	—	—	3·56
(g) Grants in-aid contribution to miscellaneous departments.	1·40	6·84	7·85	12·02
Total GRANTS	610·29	769·17	1131·51	1541·51
III. Total Expenditure of Central Govt.	646·28	693·29	782·86	914·66
IV. Percentage of I to III.	1·4	1·6	1·9	2·3

(TABLE II)
State Governments Revenue Expenditure on Scientific Departments.

(Rs. lakhs)

	1957-58	1958-59	1959-60	1960-61
Expenditure on Scientific Departments	1,06	85	1,21	1,88
Expenditure on Education	130,38	147,25	138.34	177,52
Central Grants to States for Scientific Research and Cultural Affairs.	51	1,29	200	294

5·9 There are three important quasi-Government research agencies and a Government research agency *viz.*,

The Indian Council of Agricultural Research,
The Indian Council of Medical Research,
The Council of Scientific & Industrial Research and
The Atomic Energy Commission.

all of which have contributed substantially to promotion and the expansion of research activities in India. It would be interesting to get some idea of expansion of research activities consequent on the work of these organisations.

5·10 The following table gives the growth of expenditure on research for these four institutions.

(In Millions of Rs.)

Year	I.C. A.R.	I.C. M.R.	C.S. I.R.	Sub-total (2)+(3)+(4)	A.E.C. (current)	Total (5)+(6)
(1)	(2)	(3)	(4)	(5)	(6)	(7)
1948-49	2·6	1·0	7·2	10·8	...	10·8
1949-50	2·3	1·2	11·2	14·7	...	14·7
1950-51	2·4	1·5	16·0	19·9	...	19·9
1951-52	3·9	1·3	17·8	23·0	...	23·0
1952-53	3·2	1 7	20·9	25·8	...	25·8
1953-54	5·1	1·5	19·8	26·4	...	26·4
1954-55	6·8	1·9	18·7	27·4	8·2	35·6
1955-56	6·5	2·9	22·7	32·1	15·2	47 3
1956-57	17·9	3·3	28·0	49·2	17·8	67·0
1957-58	23·7	5·7	35·5	64·9	23·8	88·7
1958-59	29·2	5·2	50 7	85·1	28·5	113·6
1959-60	35 0	7·2	61·5	103·7	30·0	133·6

The above table brings out the substantial increase so far as the combined expenditure of the four institutions are concerned. Allowing for the fact that rise in wholesale prices did not probably affect this expenditure very much, one could

compare the growth between 1948-49 and 1959-60 as a fairly good index of increase in research activities, except probably for Indian Council of Agricultural Research who undertake a good deal of expenditure on developmental activities.

5·11 The position could be more clearly indicated by representing the table in 5·10 in the from of an index as follows :

(Index 1948-49=100)

Year	I.C.A.R.	I.C.M.R.	C.S.I.R.	Sub-total (col. 5 of 5·3)	Total (Col. 7 of 5·3)
1948-49	100	100	100	100	100
1952-53	123	170	290	239	238
1955-56	250	290	315	297	439
1957-58	912	570	493	601	821
1958-59	1123	520	704	788	1052
1959-60	1346	720	854	960	1238

Even allowing for the fact that the Atomic Energy Commission probably spent a good part of their total in earlier years on construction and administrative items, the growth of expenditure on scientific research has not been insubstantial. Further, since independence there has been increasing emphasis on research even in the activities of the normal scientific and quasi-scientific departments of the Government like the Survey of India, the Geological Survey, the Indian Forest Research Institute, the Indian Veterinary Research Institute, the Central Water and Power Board etc.

5·12 International comparisons are, as already emphasised, hardly very satisfactory but are so tempting that a table* is given below for a very rough comparison :

Expenditure (Approximately) on Research

Country	% of national income	per person (converted into Rs.)
U.S.A.	1·8	154
U.S.S.R.	1·8	110
U.K.	2·1	85
China	0·4	1·1
India	0·06	0·15

* The limitations of comparability are great in this case because of differences in the content of research expenditure and also in the national income concepts, particularly for U. S. S. R.

5·13 The Council of Scientific and Industrial Research established under the First Plan 14 national laboratories

for advanced research on various subjects. Under the Second Plan 9 more institutions have been established. In the Third Plan, it is proposed to establish institutes for research in such fields as biology, petroleum technology and the development of scientific Instruments. However, as the Third Five Year Plan* states :

"There is still a wide gap between the completion of research in any field and the practical application of the results obtained. This is accounted for by a variety of reasons, such as reluctance on the part of industry and Government departments to undertake extensive trial of new processes and techniques evolved as a result of research within the country, inadequacy of pilot plant facilities, lack of designs organisations and paucity of engineers and consultants for designing and fabricating production plants. The need for eliminating these shortcomings is realised and the Third Plan will include proposals for achieving this object."

6. Development of Education in Second Plan

6·1 The Second Five Year Plan provided for a large emphasis on Basic education, Expansion of Elementary Education, Diversification of Secondary Education, Improvement of standards of College and University Education and the implementation of Social Education and Cultural Development Programme. The total outlay on Education during the second Plan was Rs. 275 crores—Rs. 68 crores in the Central Sector and Rs. 207 crores in the State Sector as against Rs. 169 crores (Rs. 44 crores at the Centre and Rs. 125 crores in the States) during the First Five Year Plan. The distribution of Outlay between States and the Centre in various fields is given below :—

(Rs. in Crores)

	Centre	States	Total
Elementary Education	4·0	88·0	92·0
Secondary Education	4·0	47·0	51·0
University Education	26·0	20·0	45·0
Technical Education	21·0	32·0	52·0
Social Education	1·0	4·0	5·0
Miscellaneous Schemes	14·0	16·0	30·0
TOTAL.	70·0*	207·0	277·0

* Includes a sum of Rs. 2 crores (approximately) for Schemes transferred from the Ministry of Rehabilitation to the Ministry of Education.

6·2 During the plan period, an expenditure of Rs. 273 crores is estimated to be incurred in various fields as under :—

* See, Chapter XXXI.

(Rs. in Crores)

	Centre	States	Total
Elementary Education	7·0	85·0	92·0
Secondary Education	3·0	43·0	46·0
University Education	25·0	21·0	46·0*
Technical Education	26·0	31·0	57·0
Social Education	1·0	4·0	5·0
Miscellaneous Schemes	14·0	13·0	27·0
Total	76·0†	197·0	273·0

* Out of this Rs. 2 Crores would be expenditure on Technical Education.

† The actual expenditure is likely to exceed the provision because of increased amounts provided for Technical Education at the time of review of annual plans.

The expenditure in the State sector is likely to go up to Rs.199 crores. The outlay and the expenditure during the plan period in various States/Union Territories is given in Statement I.

6·3 It will be observed that the expenditure in the State Sector is likely to fall short of the provision. Among the reasons for the shortfall, mention may be made of difficulty of raising matching funds for implementing Centrally Sponsored Schemes, dearth of trained and administrative personnel and heavy building content of some of the educational development programmes. Added to this is the inability of States to raise required resources, increased development expenditure outside the plan and low priority for education programmes.

6·4 The yearwise break up of expenditure by the centre and the State Governments for educational development programmes during the Second Plan is indicated below :—

(Rs. in Crores)

Year	Centre	States	Total
1956-57	6·5	17·4	23·9
1957-58	7·4	28·4	35·8
1958-59	13·2	36·3	49·5
1959-60 (R.E.)	22·5	54·1	76·6
1960-61 (B.E.)	26·4	60·8	87·2

The educational development expenditure in the Central Sector has gone up fourfold and the State sector by more than three times.

6·5 The provision of educational facilities for the Children of various age-groups and the establishment of institutions are the two main indicators of educational progress. The following statistics reveal the likely advance during the plan period.

(a) Schooling facilities for children in different age-groups.

Age-group	Facilities Available in percentages. 1955-56	Target	1960-61 Likely Achievement
6-11	51·9	62·7	61·4
11-14	16·2	22·5	23·9
14-17	8·0	11·7	12·4

Statewise deatails are given in Statement II.

(b)	Institutions	1955-56	Target	1960-61 Likely Achievement
(i)	Primary/Junior Basic	78,135	326800	341472
(ii)	Junior Basic	42,971	33800	64890
(iii)	Middle/Senior Basic	21,730	22725	38980
(iv)	Senior Basic	4,842	4571	10203
(v)	High/Higher Secondary	10,838	12125	15101
(vi)	Multipurpose Schools	365	1187	1500
(vii)	High Schools to be up-graded to Higher Secondary	—	1197	1550
(viii)	Engineering and Technology :			
	Degree Level	65	82	97
	Diploma Level	114	141	197

(See Vol. I, Ch I, table 18.)

6·6 Regional Disparities.

6·6·1. An index of educational disparity among States is the provision of educational facilities for Children of the age-group 6-11 as indicated in Statement II. In the Chapter on Education in the Report of the First Five Year Plan, it was stated,

> "There are grave disparities between different States in the matter of provision of educational facilities. The expenditure on Education compared to total revenues and population also varies in different States. The internal distribution of expenditure should be arranged and Central Grants should be so dispensed that at least the serious inequalities between States tend to disappear."

Among other things it was indicated in the Report that the need of the situation was "to help backward States by giving preferential treatment to them in the matter of grants." But not much was done to give preferential treatment to the backward states during the initial years of the First Plan. The first tangible step in this direction could be seen in the report of the First Finance Commission. The Commission kept in view the principle of equalisation and the need of assisting backward States.

> "For purpose of gauging the need for development we took as the basis the extent of the spread of primary education in the States. A good measure of this is afforded by the proportion of the children between the ages of 6 and 11, who actually attend school.................. We consider that a modest beginning should be made in the direction of helping those States where a large leeway has to be made up."
>
> (Para 13 ChapterVII)

The Commission recommended grants-in-aid to the tune of Rs. 9 crores to 8 States for the expansion of Primary education. These grants were released from the year 1953-54.

6·6·2. In the approved plan for 1955-56, provision was made for assisting the States for programmes like expansion of primary and basic education and establishment of multipurpose schools etc on the basis of matching grants. Unfortunately while formulating proposals the position of educationally backward States was not kept probably in view. The conception of matching grants for backward States had been earlier criticised by the Second Kher Committee (1950) and the International Team set up by the Government of India, in their report on Teachers and Curricula in Secondary

Schools, (1954). In spite of the recommendations contained in the first plan and the suggestions made by various Committees and Commissions, no definite steps were taken towards remedying this malady and result was that the educationally backward States remained so at the eve of the Second Plan.

6·6·3. In the Second Plan report, no specific recommendations were made for helping educationally backward States. In the course of the implementation of educational development programmes during the second plan period, the Centre sponsored a number of schemes which involved assistance on a matching basis. The Second Finance Commission which reviewed the resources position of the States *vis-a-vis* the development plans in their report opined against the system of matching grants because the State Governments were unable to meet their share of expenditure on these schemes as all their resources had already been committed for the inescapable expenditure for the implementation of the plan. (para 190). According to the Commission the matching grants may be useful in ordinary circumstances as providing a stimulus to State action in particular sphere of activity usually in the field of social services in which the Centre desires to secure Countrywide development in the national interest. They have no place when the Country has an integrated and comprehensive plan which lays down priorities for the development of all social services. The system of matching grants on any basis uniform for all States is not equitable; it operates in favour of the richer and against the poorer State. (para 191). Keeping this in view, cent per cent grant was made available to States for such schemes like 'Expansion of Girls Education and Training of Women Teachers' and 'Expansion of Primary Education and Relief to Educated Unemployed' etc. and for the first time assistance was given in relation to backwardness of the State. This has been a welcome step and is likely to assist the backward States to some extent.

6·6·4. Statement III will provide an idea whether educationally backward States have sufficient revenue resources when compared to educationally progressive States to enable them to support education. On this basis the table on page 21 will indicate the ability of States to support education and the degree of educational effort.

(The figures relate to 1958-59).

State	Ability to support Education (Rank)	Degree of Education Effort (Rank)
Assam	1	4
Mysore	2	5
West Bengal	3	2
Punjab	4	7
Bombay	5	3
Jammu & Kashmir	6	9
Kerala	7	1
Madhya Pradesh	8	4
Madras	9	5
Andhra Pradesh	10	7
Rajasthan	11	6
Orissa	12	8
Uttar Pradesh	13	11
Bihar	14	10

6·6·5. Even with the best of efforts in the Second Plan, the educationally backward States are not likely to progress much, as is indicated by the table below, which indicates the percentage of enrolment in classes I-V and VI-VIII to population in the age-groups 6-11 and 11-14 respectively.

State	Age-group 6—11	
	1955-56	1960-61
Bihar	35·7	55.3
Jammu & Kashmir	24·7	47·4
Madhya Pradesh	40 9	51·0
Orissa	34·9	50·7
Rajasthan	24·2	43·1
Uttar Pradesh	33·5	43·5

State	Age-group 11—14	
	1955-56	1960-61
Andhra	13·5	15·1
Bihar	10·3	20 0
J. &. K.	11·9	23·1
Madhya Pradesh	9·3	17·6
Orissa	7·2	8·4
Rajasthan	9·0	15·2
Uttar Pradesh	14·0	18·5

It would appear from the above that much leeway has yet to be made to bring up the backward-States to the level of the rest. The possible reasons for the backwardness of the States are as under :—

(i) Matching grants given by the Centre have perpetuated inequalities.

(ii) The educationally backward States in some cases could divert funds from education to other programmes.

(iii) In the matter of allocation of funds, low priority was given to educational programmes.

(iv) The size of the educational programme was related to the resources of the State Goverenments with the result that economically backward States could not provide more for education.

6·6·6. The educationally backward States are generally, socially and economically backward and a balance has to be struck between the priorities to be given to programmes of development of natural and human resources. In the absence of this balance, a time lag is likely to occur which may eventually hold up development in agricultural and industrial fields. A realistic view of the situation has to be taken whether it is the economic and social backwardness which is holding up educational development or it is vice versa.

6 7 *Educational Survey.*

The Ministry of Education conducted an educational survey during 1957-58. This survey was conducted for each habitation or cluster of houses, which was never attempted before even during the census, when a village (i. e. a revenue village) was adopted as the smallest unit. On 31. 3. 57, there were 8.4 lakhs habitations as against 5·3 lakhs villages. The position of the Country (except West Bengal, A. & N. Islands, L. M. & A. Islands, Pondicherry, NEFA & NHTA, which did not participate in the survey) in regard to primary schools in rural areas is summed up below :—

(Figures in lakhs)

(i) Number of Rural Habitations	8.40	% to Total
(ii) Habitations with Schools	2.29	27.2
(iii) Habitations served by Schools in neighbourhood	3.71	44.1
(iv) Habitations not served by Schools	2.40	28.7
	8.40	100.0

6·8 Expansion of Primary Education.

A scheme for the appointment of 60,000 teachers during the Second Plan was initiated in 1958-59. Under the scheme the Central Government pay financial assistance to the States on cent percent basis for (a) emoluments of teachers to be appointed under the scheme. (b) equipment grant @ Rs. 250 per teacher (c) training of teachers (d) experiments in introducing compulsion (e) appointment of 12000 inspecting officers of the lowest rank. The distribution of teachers to the States and Union Territories is worked out in proportion to the number of Children of 6·14 not attending Schools.

6·9 Expansion of Girls Education.

The low percentage of girls attending schools is a big bottleneck in the expansion of Elementary Education. To overcome this drawback, the Central Government initiated during the Second Plan a scheme for the Expansion of Girls Education and Training of Women Teachers with an outlay of Rs. 2.4 crores. The Central assistance is made available to the States for the opening of new girls schools, training of Women Teachers, provision of attendance scholarships for girl student and teachers training of 3-5 years duration for girls etc. The Central assistance is worked out in proportion to the number of girls in the age-group 6-14 not attending Schools.

6·10 Training Programme of Teachers.

For an adequate supply of trained primary school teahers, the Ministry of Education initiated in 1959-60 a scheme to expand facilities for teachers training with 100% financial assistance to States/Union Territories. The estimated expenditure on the scheme during Second Plan is Rs. 4 crores.

6·11 Basic Education.

Although there is likely to be considerable expansion in this field during the plan period, doubts have been raised whether the basic system of education is proceeding on the right lines. The Assessment Committee on basic Education (1956) listed *inter-alia* the following factors responsible for slow progress of Basic education.

(i) Basic schools are conducted as isolated units surrounded by huge areas of ordinary schools.

(ii) Those incharge of administering Basic education have no understanding, faith or trainnig in Basic education.

(iii) In good number of basic schools, craft equipment and craft materials were either lacking or did not reach individual schools in time,

(iv) Training of Basic teachers in training institutions was far from satisfactory.

(v) Most of the basic schools were only 5 grade schools.

(vi) Most of the teachers in basic schools are trained in old methods and have not sufficient training in Basic education.

These are some of the difficulties which are retarding the qualitative progress of Basic education.

6·12 Secondary Education.

There has been rapid expansisn of schooling facilities at this stage. However, in the case of girls the expansion has not been very much marked as indicated below :

Enrolment in classes IX-XI as percentage of the Population in the group 14-17

	1955-56	1960-61 (Estimated)
Total	8·0	12·4
Boys	13·0	19·2
Girls	2·8	5·4

The implementation of the recommendations of the Secondary Education Commission initiated in the First Plan has continued during the Second Plan also. By the end of the Second Plan there are likely to be 1550 multipurpose schools as against 365 in the beginning. Similarly the number of Higher Secondary schools by 1960-61 would be 1500 as against 77 in 1955-56. There are considerable variations in respect of the establishment of multipurpose schools from State to State. Shortage of teaching personnel continued all round. In the vocational subjects teachers are not available in the scales of pay offered. Though a number of State Governments have established educational and vocational guidance bureaus they have not succeeded in reaching the schools to a large extent. The paucity of text books in multipurpose schools is acutely felt. The expansion of Secondary Education without any proportionate increase in the provision of facilities such as libraries, laboratories etc. has brought down the standards materially. Only 48·2% of the students passed the Matriculation and equivalent examination in 1957-58.

6·13. University Education.

No definite targets of expansion were laid down for this field in the Second Plan. None the less the number of students in Colleges and Universities excluding the pre-

University Class is expected to rise from 5·3 lakhs in 1955-56 to 7·2 lakhs in 1960-61. In the absence of proportionate increase in physical facilities, the increasing numbers has led to overcrowding and fall in standards etc. The percentage of failures is very high and leads to wastage. With the establishment of U. G. C., development grants have been made to Universities and Colleges for programme of improvement such as three-year degree Course, scholarships, students welfare, students home. An important measure taken up by the U. G. C. and the Central Government during the Second Plan period is to improve the salary scales of University and College teachers.

6·14 Technical Education.

An Expenditure of Rs. 59 crores is likely to be incurred on Technical education programme, out of the total provision of Rs. 275 crores. The corresponding expenditure in the first plan was Rs. 20 crores. During the Second Plan, the proportion of development expenditure on Technical Education, was comparatively much larger than first plan.

Year	Development Expenditure on Education	Development Expenditure on Technical Education.	Col. 3 as% of Col. 2
(1)	(2)	(3)	(4)
	(Rs. in crores)		
1951-56	152·9	20·2	13·2
1956-61	273·0	59·0	22·0

As a result of the various measures, there has been considerable expansion in the provision of facilities for technical education as indicated below :—

Technical Institutions—Engineering Colleges and Polytechnics—Intake and Out-Turn

Year	Eng. & Tech. Colleges			Polytechnics		
	No.	Intake	Out-turn	No.	Intake	Out-turn
1956	74	6632	4293	111	10242	4075
1957	74	9778	4290	129	15995	5034
1958	83	11096	4665	157	19332	6345
1959	86	11432	4750	166	21097	9900
1960*	97	13498	5310	193	25291	10397

* Estimated, See, Third Five Year Plan, p. 615.

6·15 Literary.

A very rough measure of social efficiency of a pepole is the percentage of literates among them. No targets of literacy were laid down in the Second plan. As a result of the various educational measures, the literacy is estimated to rise from 20 percent in 1951 (30 percent in case of men and 9 percent in case of women) to 28 percent (41 percent in case of men and 13 percent in case of women). But it will be long before cent percent literacy can be attained.

STATEMENT I—(For Para—6·2)

Expenditure on Education in Second Plan

State/Union Territory	Plan Outlay (1956-61)	Estimated Expenditure (1956-61)	Excess (+) Shortfall (—)
	(Rupees in Lakhs)		
Andhra Pradesh	1264·23	1182·57	(—) 81·66
Assam	714·71	713·00	(—) 1·71
Bihar	2283·08	1908·45	(—) 374·63
Gujarat } Maharashtra }	2296·71	1020·05 } 1524·54 }	(+) 247·38
Jammu & Kashmir	285·00	202·57	(—) 82·48
Kerala	1010·49	1028·00	(+) 17·51
Madhya Pradesh	2062·80	1494·66	(—) 566·14
Madras	1153·98	1336·28	(+) 182·30
Mysore	1188·07	1106·94	(—) 81·13
Orissa	638·12	648·67	(+) 10·55
Punjab	1477·17	1024·23	(—) 452·94
Rajasthan	1056·25	1406·67	(+) 350·42
Uttar Pradesh	2654·19	1761·28	(—) 892·91
West Bengal	2216·56	2722·89	(+) 506·33
A. & N.Islands	27·40	13·75	(—) 13·65
Delhi	380 00	412·67	(+) 32·67
Himachal Pradesh	114·00	71·78	(—) 42·22
Manipur	57·00	67·71	(+) 10·71
N. H. T. A.	12·22	49·90	(+) 37·68
Tripura	112·16	128·97	(+) 16·81
L. M. &. A. Islands	12·40	12·19	(+) 0·21
N. E. F. A.	50·00	63·47	(+) 13·47
Pondicherry	58·65	32·10	(—) 26·55
TOTAL	21125·19	19933·34	(—)1191·85

STATEMENT II—(for Para—6·6·1)

Schooling Facilities for Various Age-Group*

(In Percentages)

State/Union Territories	6—11		11—14		14—17	
	1955-56	1960-61	1955-56	1960-61	1955-56	1960-61
Andhra Pradesh	56·7	58·2	13·5	15·1	8·4	8·5
Assam	59·4	60·6	21·9	31·3	11·6	18·1
Bihar	35·7	55·3	10·3	20·0	5·9	12·8
Maharashtra	66·5	70·8	18·1	26·7	8·6	12·3
Gujarat		64·0		47·6		23·9
Jammu & Kashmir	24·7	47·4	11·9	23·1	5·5	7·6
Kerala	109·1	107·0	36·8	49·4	19·5	21·2
Madhya Pradesh	40·9	51·0	9·3	17·6	3·0	4·7
Madras	66·4	74·3	21·3	28·2	9·3	12·6
Mysore	57·8	71·9	16·5	23·3	9·2	10·2
Orissa	34·9	50·7	7·2	8·4	2·9	4·4
Punjab	56·6	63·4	25·8	29·7	11·3	13·8
Rajasthan	24·2	43·1	9·0	15·2	4·1	7·6
Uttar Pradesh	33·5	43·5	14·0	18·5	7·6	12·1
West Bengal	73·6	77·3	19·4	26·3	9·1	16·3
A. & N. Islands	63·3	92 0	15·8	13·3	0·5	10·0
Delhi	78·4	93·9	48·5	62·6	18·6	51·3
Himachal Pradesh	47·4	59·4	16·4	37·5	5·2	10·2
Manipur	87·3	64·7	19·7	35·5	10·9	9·5
Tripura	62·2	81·0	19·2	36·3	7·3	1·3
L.M. & A. Islands	69·6	50·0	2·0	10·0	—	—
NEFA	6·2	7·9	0·9	1·3	1·5	0·7
Pondicherry	49·6	84·1	13·9	27·7	3·4	11·0
India	51·9	61·4	16·2	23·9	8 0	12·4

* The figures have been worked out by relating the enrolment in Classes I-V, VI-VIII and IX-XI to population of the respective age-groups ; see, however, Third Five Year Plan, pp. 604—606.

STATEMENT III—(for para 6·6·4)

Revenue and Expenditure on Education, 1958-59

State	Populaton* (in Lakhs)	Total Revenue in Lakhs of Rs.)	Revenue per 10,000 of Population in 000's Rs.	Rank	State Govt. Expenditure on Education (in Lakhs)	Exp. per 10,000 of Population (in 000's Rs.	Rank	State Govt. Exp. on education as percentage of Revenue	Rank
1	2	3	4	5	6	7	8	9	10
Andra Pradesh	358·5	6752	188	10	1187	33	7	17·6	6
Assam	105·3	3197	304	1	437	42	4	11·0	13
Bihar	436·5	6094	140	14	1051	24	10	17·2	7
Bombay	568·5	14116	248	5	2629	46	3	18·6	5
Jammu & Kashmir	51·0	1129	221	6	128†	25	9	11·3	12
Kerala	163·6	3521	215	7	976†	60	1	27·7	1
Madhya Pradesh	289·7	6062	209	8	1231	42	4	28·3	2
Madras	346·2	6995	202	9	1423	41	5	20·3	2
Mysore	230·0	6889	299	2	944	41	5	13·7	9
Orissa	160·6	2748	171	12	427	27	8	15·5	8
Punjab	189·8	5022	265	4	618†	33	7	12·3	11
Rajasthan	188·0	3397	181	11	665	35	6	19·6	3
Uttar Pradesh	716·8	11723	164	13	1563	22	11	13·3	10
West Bengal	288·7	8039	278	3	1514	52	2	18·8	4

* 1. Source* C. S. O.; on population in inter-census years See Vol. I, Ch. II, para 6.

·2 See Vol I, Ch. I Tables 16 and 17.

† Figures relate to 1957-58.

7. Education in the Third Five Year-Plan.

7·1 It is necessary to analyse the programmes of education in detail in the Third Five Year Plan. Article 45 of the Constitution of India laid down the directive principle regarding provision for free and compulsory education for children while Article 41 enjoined that effective provision be made for securing the right to education. The Constitution of India, therefore, recognised the self-evident proposition that the system of Education has a significant influence on the rate of development in a Country—economic and social. To ensure any steady move forward, it is necessary to ensure a rapid expansion of educational facilities culminating in the introduction of Universal and Compulsory education. So great is the significance of this factor that thinkers in all ages have recognised its importance and as Alfred Marshall put it "no change would conduce so much to a rapid increase of national wealth as an improvement in our Schools and specially of middle grades; provided it could be combined with an extensive system for scholarships, which will enable the clever son of a working man to rise gradually from school to school till he has the best technical and productive education which the age can give."

7·2 In planning the most pressing problem is that of priorities—priority amongst the different stages of education and the needs and claims whithin each stage. The claims of these stages are really complementary and integrally inter-related, but when they have to be assessed in the context of inadequate resources, they are apt to become competitive. We have in the last two plans adopted a programme of expansion for the primary stages; the emphasis in other stages of education—secondary, social and University was primarily on the improvement of quality, the raising of standards and a closer adjustment of the contents of education to individual and social needs. In the programme of Education, included in the Third Plan, the emphasis is on the provision of facilities for Universal education for the age-group 6-11, improvement of science education at the Secondary and Universisy stages, training of teachers of all grades and expansion of technical education.

7·3 The total outlay on educational programmes including those relating to technical education, during the Third Plan is estimated to be about Rs. 569* Crores against an

* The figure has been worked out from the preliminary estimates of physical targets. The Third Plan gives a total outlay of Rs. 500 crores approximately as financial outlay. See Third Five Year Plan chapters XXIX to XXXI.

anticipated expenditure of Rs. 273 crores during the Second Plan. This includes Rs. 413 crores for general education and cultural programmes and Rs. 168 crores for technical education compared to Rs. 214 crores and 59 crores respectively in the Second Plan. The break up of estimated outlay between Central and State sectors is Rs. 167 crores and Rs. 402 crores as against Rs. 76 crores and Rs. 197 crores respectively in the Second plan. The distribution ef outlay between different fields of education in the Second and Third Plan is given below:—

(TABLE for 7·3)

Group	Estimated Expenditure during Second Plan	Percentage to total	Anticipated outlay on Third Plan	Percentage to total	Percentage Increase of (4) over (2)
(1)	(2)	(3)	(4)	(5)	(6)
		(Rs. in Crores)			
Elementary Education	92·0	33·7	203·0	35·7	120·7
Secondary Education	46·0	16·9	87·0	15·3	89·1
University Education	44·0	16·1	78·0	13·7	77·3
Technical Education	59·0	21·6	156·0	27·4	164·4
Miscellaneous (including Social Education & Cultural Programmes.	32·0	11·7	45·0	7·9	40·6
Total	273·0	100·0	569·0	100·0	108·4

7·4 Statement I provides an idea of the estimated outlay on Education in various fields during the Third Plan indicating estimates of Statewise outlay.

7·5 With the implementation of the educational development programmes in various States during the Third plan period, the number of children of various age-groups in schools is likely to go up considerably by 1965-66 as under :

(For details see statement II).

Age-Group	Estimated Enrolment in 1960-61	Estimated Enrolment in 1965-66	Additional Enrolment	%Increase
		(Figures in lakhs)		
6-11	337	482	145	43·0
11-14	58	100	42	72·4
14-17	30	53	23	76·7

The above figures suggest that the efforts made so far and those envisaged in the third plan are by no means small. They have, however, to be seen against the background of the magnitude of the problem which brings out the still enormous tasks to be carried out.

7·6 Elementary Education.

7·6·1. In a Welfare State, it is of paramount importance that every citizen receives at least the basic quantum of primary education. Ignorance not only prevents the democratic ideal from being fully realised but also acts as a break on social growth and economic advancement. In fact it will not be wrong to say that because of lack of elementary education, the full benefit of reforms in other spheres of life may not be realised by the nation. It is estimated that by the end of the Second plan about 61% of the children in the age-group 6-11 will be undergoing schooling. But there is still a marked disparity between boys and girls attending schools, although this is steadily diminishing. It is mainly because of this factor and because some areas are especially backward that the proportion of children of 6-11 attending schools by the end of third plan may not exceed 80 per cent. In the case of boys it should be possible to ensure almost universal coverage but in the case of girls the percentage may not go beyond 60 percent. Similarly the proportion of pupils in the age-group 11-14 will have risen to about 24 percent by the end of Second plan period. In this group also the disparity between boys and girls is considerable. With the execution of elementary education expansion programme, the percentage of pupils of age-group 11-14 is likely to rise to 30 percent by 1965-66. For this age-group regular schooling facilities are proposed to be supplemented by opportunities for continuation of education. Besides, the Ministry of Labour and Employment are working out a scheme for providing technical training of a simple character for children who have received education up to the age of 11 years.

7·6·2 The Assessment Committee on Basic education (1956) recommended that the system of areas should no longer be the sole method of expansion of Basic education. Instead the entire field of elementary education should be subjected to a programme of gradual conversion to basic pattern so as to make them properly receptive to change when it comes to them. Such an orientation programme has already been initiated in the second plan and will be carried forward in the Third plan. But in view of the large number of schools involved and the fact that the majority of the existing teachers have not had training in Basic education, progress towards fully developed basic schools will of necessity be spread over a long period. These schools will take up such activities as can be carried out with maximum community effort and with the measure of State assistance that can be made available for the purpose under the plan. The orientation programme requires large number of basic trained teachers. The emphasis on teacher training on basic lines is considerably being increased in the Third plan so that by the end of the plan period all training institutions will be of basic type as against 70% by the end of Second plan. To improve the quality of teaching, the period of training for elementary school teachers is proposed to be extended to two years besides provision of liberal facilities in respect of equipment and library.

7·6·3. Progress towards Basic education will largely depend on the steps taken to remove the limitations of existing basic institutions. This *inter-alia* calls for much effort in ensuring adequate training, improvement in teaching methods, efficient inspection, provision of suitable literature and conscious efforts to link the activities of basic schools with those of the local community in the field of agriculture, village industries, community development, social education etc. To work out effective links between the school and local development activities, it is proposed to establish model senior basic schools in the selected development blocks. A feature of the past programme in the expansion of Basic education has been that it was largely confined to rural areas. A number of model basic schools are, therefore, proposed to be set up in urban areas during the third plan period.

7·6·4. Education of girls is posing a problem all over the country but is of formidable magnitude especially in Madhya Pradesh, Rajasthan, U.P., Jammu & Kashmir, Bihar and Orissa. With a view to tackling this problem special efforts are being adopted and the measures for the promotion of girls' education that are proposed to be implemented during the third plan period are :

(i) Free tuition for girls.

(ii) Attendance scholarships and prizes.

(iii) Free supply of books, stationery and clothing.

(iv) Separate part-time and continuation classes for girls.

(v) School mothers in co educational institutions where there are no women teachers.

(vi) Hostels for girls.

(vii) Free residential accommodation for women teachers in rural areas.

7·7 Secondary Education.

7·7·1. The three main directions in which it is proposed to continue the reorganisation of Secondary education during the Third plan are: (a) to increase facilities for science education (b) to improve the multipurpose schools established during the Second plan and increase their number to a limited extent and (c) to set up new secondary schools as higher secondary institutions and to convert existing secondary schools to this pattern to the extent feasible. By the end of the Second Plan facilities for science education are likely to be available in about 11500 schools. During the third plan it is proposed to extend this facility to 4000 new secondary schools to be opened during this period in addition to the remaining 3500 secondary schools. Besides, science as an elective subject is to be introduced in as many schools as possible. Apart from the provision of laboratories, the main difficulty in expanding science teaching is the lack of adequately trained teachers. In this connection a number of suggestions have been made by the All India Council for Secondary Education *e.g.*, special training schemes for science teachers and laboratory assistants, preparation of standardised designs of science apparatus and arrangements for the distribution of equipment among educational institutions, which are likely to be implemented by the States.

7·7·2. So far as multi-purpose schools are concerned, because of the difficulty of obtaining trained teachers especially for subjects requiring practical instruction, the main emphasis in the third five year plan has been put on improving the institutions already set up apart from opening a limited number of new multipurpose schools. To cope with the requirements of teachers, four regional training colleges are proposed to be set up. It is estimated that during the plan period 2000 existing high schools will be upgraded to higher secondary standard besides opening 4000 new higher secondary schools.

7·8 University Education.

7·8·1 It is generally recognised that, to a large extent, the success of democracy depends upon a selfless, intelligent and well-informed leadership which is a direct consequence of high standards of general, vocational and professional education. Dissemination of learning, incessant search for new knowledge and provision of specialised instruction to satisfy the occupational needs of society are the vital tasks of higher education. Universities in India because of their long history, have to maintain a link between tradition and experiment, between the values of the past and the challenges of the future. As repositories of culture and pioneers in blazing new trails, the Universities have the responsibility of evolving courses which reflect the many side of Indian life and provide a meeting ground where the achievements of our own people can be combined with the knowledge and experience of the outside world. In mundane terms, all this implies the necessity of assuring increased provisions.

7·8·2 During the third plan, the programmes initiated in the second plan for qualitative improvement and improvement of teacher-pupil ratio, grants for research and publications, organisations of seminars and provision of amenities for students will be continued and additional facilities provided in numbers as well as for improvement. It has been suggested that admissions should be regulated on the basis of adjudged capacity of students to benefit from such education but this would be possible only after the techniques of guidance, examination and selection have been perfected and this alone may take years of planned effort. Till then allowance has to be made for the normal expected increase. The programmes to be undertaken in the Third plan include provision of facilities for science teaching, raising of the scales of pay of teachers, improvement of laboratories and libraries, provision of post graduate studies and research scholarships and loans, assistance for hostel and staff quarters and other schemes such as rural institutes, evening colleges, correspondence courses and pilot projects. One of the main tasks in the Third plan will be to expand facilities for the teaching of science, the aim being to raise proportion of science students to about 40 percent. This has been necessitated to meet the increasing demand in a number of different fields—science teachers for schools, students for engineering and other technical institutions, industries etc.

7.8·3. To improve the content of education at the University Stage, the measures initiated by the University

Grants Commission in the Second plan such as introduction of three year degree course, improvement of laboratories and libraries, development of post graduate studies and research, institution of merit and research scholarships, improvement of salary scales of teachers etc. etc. will be continued during the Third plan. The U. G. C. assists the Universities for Development Schemes for five years after the inception of the scheme. Thereafter it is the responsibility of the University to meet the expenses from their own sources.

7·9 *Miscellaneous.*

The other programmes included in the Third plan include intensification of a social education, development of languages and culture, youth programmes and the establishment of the National Central Reference Library. To improve the content of education so far as moral and social values are concerned, the plan includes schemes for the preparation of suitable texts designed to stimulate interest and faith in moral and social ideals, the imparting of moral instruction and arrangements for organised social service involving participation in community work.

7·10 *Technical Education.*

7·10· 1. It is a well established fact that technological advance is necessary for any economic development in the increasingly complex industrial and social organisation towards which modern society has been moving. As long as a nation educates only a small proportion of its children the instruction given could be only of a special or liberal kind for men who on account of their means were able to get an exclusive and costly liberal education. But when a nation decides to take to school almost all its young people upto the age of 14, it is most important that education given in later years should be appropriate. Otherwise large numbers may be prepared for a type of life which they will not be able to lead. Facilities for vocational training on a large scale here will have their significant function. During the lifetime of young children for whom we are making elementary education free and compulsory, the spread of technology in this country will have changed the very values and ways of living.

7·10· 2. During the second plan, significant advance has been made in the field of technical education. The Third Plan envisages an outlay of Rs. 156 crores in this field against Rs. 59 crores in the Second Plan. During this period, it is proposed to increase the annual intake of degree students by

about 4000 to 17,500 and of diploma holders by about 9000 to 34000. This increase will be brought about by the expansion of admission facilities in the existing institutions and opening of new ones. During the period 1961-66, 14 new colleges and 41 new polytechnics are likely to be established in addition to 49 junior technical schools as adjuncts to Polytechnics, in various States. Statement III gives a state-wise account of the additional institutions to be established and the additional intake in institutions of various standards during the plan period.

7·10·3. Besides the setting up of new engineering institutions, the main programmes in the field of technical education relate to the development of school of Mines and Applied Geology, Dhanbad, Delhi Polytechnic, the Indian Institute of Technology, Kharagpur and the other Institutes of Technology set up in Bombay, Madras and Kanpur during the Second plan. The existing four schools of Printing and the Institute of Town and Country Planning will be further developed. The schemes relating to Practical Training Stipends and Research Training Scholarships will be continued. The continuation programme of the 8 Regional Engineering Colleges and 27 Polytechnics and the expansion of facilities in selected institutions initiated in the second plan will be completed. The five year integrated course in engineering/technology will be introduced in a number of institutions. Provision has also been made for replacing the obsolete equipment and for improving the ill-equipped engineering institutions. The programme also provides for scholarships, hostels and improvment in the salary scale of teachers.*

7·10·4. Shortage of teaching personnel is a stumbling block in the expansion of technical education. The schemes of training fellowships in selected engineering colleges and foreign studentship for graduates who return to teaching posts initiated in the Second plan will continue in the Third plan. Coupled with this, the higher salary scales recommended by the All India Council for Technical Education is expected to attract large numbers to this profession and ease the situation to a great extent.

* For a distribution of technical institutions by States see Third Five Year Plan, p. 615.

STATEMENT I—(for para 7·4)

Estimated outlay on Education in the Third Five-Year Plan*

State/Union Territory	General Education					Cultural Programme	Technical Education	Total Education
	Elementary Education	Secondary Education	University Education	Other Education Scheme	Total			
								(Rs. in Crores)
Andhra Pradesh	12·16	5·50	1·96	0·94	20·56	0·02	3·55	24·13
Assam	9·01	2·99	0·85	0·65	13·50	0·19	2·70	16·39
Bihar	19·45	7·14	5·39	1·69	23·67	0·36	5·04	39·07
Gujarat	8 64	3·15	1·65	0·84	14 28	0·17	3·07	17·52
Jammu & Kashmir	2·07	0·93	0·43	0·32	3·75	0·23	1·00	4.98
Kerala	7·27	5·04	1·19	0·82	14·32	0·32	3·79	18·43
Madhya Pradesh	18·25	4·68	3·04	0·82	26·79	0·26	5·00	32·05
Madras	10·00	6·09	0·56	0·78	25·43	0·21	6·52	32·16
Maharashtra	9·91	3·92	3·09	0.33	17·25	0·19	5·65	23·09
Mysore	10·62	3·09	1·50	0·82	16·02	0·18	5·00	21·20
Orissa	10·80	2·14	1·45	0·66	15·05	0·09	2·15	17·29
Punjab	7·37	6·74	2·63	1·26	18·00	0·16	5·80	23·96
Rajasthan	10·58	3·75	2·32	0·85	17·50	0·29	3·50	21·29
Uttar Pradesh	33·85	7·00	5·85	2·22	48·92	0·30	8·80	58·02
West Bengal	11·37	5·31	4·48	1·74	22·90	0·35	6·04	29·29
A. & N. Islands	0·37	0·14	0·03	0·03	0·57	—	—	0·57
Delhi	6·15	4·86	—	0·43	11·44	—	1·56	13·09
Himachal Pradesh	1·08	0·33	0·23	0·08	2·02	—	—	2·02
L. M. & A. Islands	0·11	0·06	—	0·02	0·19	—	—	0·19
Manipur	0·60	0·39	0·04	0·11	1·14	—	0·04	1·18
N. E. F. A.	0·49	0·31	0·01	0·01	0·82	—	—	0·82
N. L. T. A.	0·65	0·25	0·07	0·03	1·00	0·02	—	2·47
Pondicherry	0·51	0·46	0.22	0·18	1·37	—	0·20	1·57
Tripura	1·50	0·20	0·20	0·19	2·31	—	0·19	1·02
Total (States)	200·81	73·98	37·19	15·82	328·80	3·34	96·66	461·80
Central Schemes	2·45	11·98	40·50	17·18	72·07	8·41	86·62	167·09
Total (India)	203·26	86·92	77·69	33·00	400·87	11·75	156·57	568·89

*Tentative, based on targets.

STATEMENT II—(for Para 7.5)
Enrolment during the Third Five Year Plan*

State/ Union Territory	6-11 Additional Enrolment	6-11 Total by 1965-66	11-14 Additional Enrolment	11-14 Total by 1965-66	14-17 Additional Enrolment	14-17 Total by 1965-66
1	2	3	4	5	6	7
			(Figures in lakhs)			
Andhra Pradesh	16.00	44.20	2.58	6.13	0.50	2.36
Assam	4.40	15.06	0.50	2.66	0.28	1.33
Bihar	16.00	48.00	3.75	9.25	1.90	5.00
Gujarat	8.00	24.00	N.A	N.A	1.42	4.20
Jammu & Kashmir	1.36	3 33	0.28	0.76	0.06	0 21
Kerala	3.08	26.52	1.83	7.27	0.30	2.55
Madhya Pradesh	10.00	30.00	1.70	4.96	0.82	1.58
Madras	11.83	45,54	3.00	9.36	1.30	3.97
Maharashtra	8.22	47.14	12.36	19.14	7.70	10.57
Mysore	10.00	31.44	3.73	7.46	0.72	2.19
Orissa	6.00	16.00	0.85	1.70	0.40	0.80
Punjab	6.00	22.86	1.80	5.60	0.80	2.43
Rajasthan	8.00	19.50	1.94	3.85	0.67	1.53
U.P.	26.07	66.30	3.50	11.60	2.28	7.40
West Bengal	7.00	34.47	3.94	8.94	3.57	6.51
A.&.N. Islands	0.02	0.06	0.01	0.02	N.A.	N.A.
Delhi	1.13	3.24	0.60	N.A.	0.38	N.A.
Himachal Pradesh	0.34	1.17	0.09	0.32	0.03	0.08
L.M.&.A. Islands	0.01	0.05	0.01	0.01	0.0 (450)	0.01 (500)
Manipur	0.30	0.88	0.03	0.17	0.02	0.05
N.E.F.A.	0.10	0.16	0.01	0.02	0.0 (300)	0.01 (500)
N.H.T.A.	0.06	0.17	N,A.	N.A.	N.A.	N.A.
Pondichery	0.12	0.47	0.02	0.10	0.03	0.06
Tripura	0.50	1.31	0.13	0.27	0.04	0.08
India	144.54	481.87	42.66	99.59	23.22	52.92

* Estimated ; see, however, Third five year Plan, pp. 604-606.

STATEMENT III—(for Para 7.10.2)

Additional Institutions and Seats during* Third Plan.

State/ Union Territories	Additional Institutions			Additional Seats		
	Degree	Diploma	Junior Technical Schools	Degree	Diploma	Sandwich course
Andhra Pradesh	—	1	—	—	180	—
Assam	1	1	6	310	240	—
Bihar	—	5	—	134	1080	—
Gujarat	1	2	—	250	360	—
Jammu & Kashmir	—	—	—	—	—	—
Kerala	1	1	—	340	490	—
Madhya Pradesh	1	5	10	300	510	—
Madras	1	2	20	610	700	—
Maharashtra	2	5	—	400	800	—
Mysore	—	—	—	210	300	—
Orissa	1	2	—	310	300	—
Punjab	1	4	—	370	660	120
Rajasthan	1	2	—	365	450	—
Uttar Pradesh	1	5	8	240	1800	—
West Bengal	3	4	1	300	720	350
A.&.N. Islands	—	—	—	—	—	—
Delhi	—	2	4	—	480	—
Himachal Pradesh	—	—	—	—	—	—
L.M.&.A. Islands	—	—	—	—	—	—
Manipur	—	—	—	—	60	—
N.E.F.A.	—	—	—	—	—	—
N.H.T.A.	—	—	—	—	—	—
Pondicherry	—	—	—	—	—	—
Tripura	—	—	—	—	—	—
India	14	41	49	4139	9130	470

* Tentative Estimates.

8. Medical and Public Health.

8.1 Second only to requirements of education, come the requirements of health of the people. In fact, the acceptance of the ideology of a Welfare State logically implies the acceptance of the idea of medical relief ceasing to be the perquisite of a few, and becoming the right of the many. Item 6 of the State List (List II, Seventh Schedule of the Constitution of India) makes "Public Health and Sanitation ; hospitals and dispensaries", State subjects. It would, therefore, appear that Union Government have little direct responsibility in regard to health ; but, it would be unwise to, therefore, simply confine its activities to "co-ordination, the Collection and supply of information, supply of technical assistance and advice, and such other assistance as can be given for the promotion of the health and well-being of the Country." A more dynamic approach is necessary, for, as Raj Kumari Amrit Kaur[7] put it :—

"Disease knows no barriers. Likewise, measures against it can have no barriers, international or provincial. Health measures must, therefore, be all embracing and cover every part of India".

8·2 In India, as perhaps in all countries of the world, sections of the population live under conditions which are generally considered unsatisfactory and which consequently ought to be improved. There is widespread agreement on the importance of health as a component in the level of living, and, in every country there is unquestioned acceptance by the State of its responsibility in this respect, the Constitution of India recognising (Article 47) the improvement of public health as a primary duty of the State.

8·3 The Third Five Year Plan divides health programme into six broad categories :—

(1) Improvement of environmental hygiene, specially rural and urban water supply ;

(2) Control of communicable diseases ;

(3) Provision of adequate institutional facilities to serve as a base for organising health services ;

(4) Provision of facilities for the training of medical and health personnel ;

(5) Family Planning ; and

7. p. XIV, Health in Independent India (Ministry of Health, New Delhi, (1957).

(6) Public health services, including maternal and child welfare, health, education and nutrition.

8·4 The table given below shows the distribution of outlay under different heads under the three plans :

Outlays on Health Programmes (Rs. crores)

Programme	First Plan	Second Plan (anticipated outlay).	Third Plan (Proposed outlay).
1. Water supply and sanitation (Rural and Urban).	49.0	72.0	80.0
2. Primary Health Units, hospitals and dispensaries.	25.0	37.0	50.0
3. Control of communicable diseases.	23.1	69.0	92.0
4. Education and training.	21.6	35.0	38.0
5. Indigenous system of medicine.	0.4	4.0	8.0
6. Family planning.	0.7	3.0	25.0
7. Other schemes.	20.2	5.0	7.0
8. Total.	140.0	225.0	300.0
Percentage increase over first Plan.	—	60	
Percentage increase over second Plan.		—	33

8.5 The Third Plan proposes to place greater emphasis on preventive public health services and on the eradication and control of communicable diseases. The programmes initiated during the first two plans would be continued in the third plan. The programme in the third plan includes the establishment of field training and demonstration centres, setting up of health education bureaux in States in which these do not at present exist, training of health education specialists, formation of social education units, organisation of health education services and the production of health education material.

The following groups have been indicated as requiring special care :—

(a) expectant and nursing mothers, and, infants ;
(b) school going children.

8.6 Revenue Expenditure on Medical and Public Health.

(Rs. lakhs.)

	1956-57	1957-58	1958-59	1959-60 R.E.	1960-61 B.E.
I. Centre. —	6,22	13,21	13,41	17,18	20,85
II. Total expenditure of the Centre.	500,52	658,86	706,42	795,35	890,13
Percentage of I to II.	1.2	2.0	1.8	2.2	2.3
III. States—	47,86	51,58	58,00	74,50	83,14
IV. Total Expenditure of States.	644,58	689,57	768,40	872,25	949,01
Percentage of III to IV.	7.4	7.5	7.5	8.5	8.7
V. Centre's Grant to States for Medical and Public Health.	3,89	6,53	10,79	12,49	19,77

8.7 Since in matters of health facilities, financial outlay is not always a clear indication of the progress of facilities, the table given below attempts a quantitative evaluation :

No. of Hospital, Patients treated and Doctors-

S. No. Items.	1950	1951	1955	1957	1958
1. No. of Hospitals.	2,641	2,694	2,966	2,733	3,407
2. No. of Dispensaries.	6,803	6,515	6,539	7,275	6,567
3. No. of Beds.	111,512	117,178	138,804	144,762	164,127
4. No. of patients treated (in Million Nos.)	82.4	100.8	134.3	124.7	126.9
(a) Indoors. (In million Nos.)	3.2	3.5	8.6	6.0	6.9

—*Continued*

S. No. Items	1950	1951	1955	1957	1958
(b) Outdoors. (In million Nos.)	79.2	97.3	125.7	118.7	120.0
5. Registered Medical Practitioners.	59,338	61,480	70,152	75,448	78,258
6. Patients treated per-medical practitioner.	1,388	1,639	1,914	1,653	1,621
7. Indoor patients per bed.	29	30	62	41	42

(For details See Vol. I, Ch I, Tables 20 and 21).

8·7 Any continuing scheme of improvement in facilities relating to health, must necessarily imply an increasing provision for Medical Education—the position in respect of which is indicated in the table below :—

Medical Education (Numbers)

S. No. Items	1950-51	1951-52	1955-56	1957-58	1958-59	1959-60
Medical Colleges.						
1. Colleges.	30	30	40	48	51	55
2. Pupils admitted.	2,676	2,521	3,560	4,091	4,554	4,904
Dental Colleges.						
1. Colleges.	4	4	6	7	7	10
2. Pupils admitted.	83	85	178	202	230	350

8·8 A primary indicator of health conditions in a country is the expectation of life at birth, and, both its absolute level and its trend over time is usually taken to show improvements in health conditions. In this connection a series of official life tables are available for a number of census decades, and, some of the gaps have been filled up by the work of individual research experts. The position in India has been indicated in Volume I, Chapter II, Para 2·4.

8·9 An important index of improved health measures is a declining death rate, especially a decline in the rate of infant mortality, problems relating to which have been discussed in Vol I, Chapter II, paras 2.3, 2.5 and 3·2·2.

8·10 The very first consideration in any large scale scheme for raising the standards of health of the nation is to make available to the people of the country adequate and

properly balanced nutritive food. However, in an economic system based on personal earnings and consumption-purchase, the supply of adequate nutrition is essentially a question of raising the incomes and standards of living of the individuals, especially those who are living on the verge of bare subsistence. The Prime Minister has stated[8] :—

> "Poverty and health do not go together............... ..... A war on disease and ill-health is, therefore, essentially a war on poverty and all its evil brood. In effect, it is the raising of the standards of the nation in every way, and we come back to our Five Year Plans whose aim it is to do this."

8·11 How much is spent on medical facilities by the poor citizen in India ? This is an important question since, in spite of the growing expenditure by the State on medical facilities, the bulk of the cost of medical treatment must fall on the personal expenditure of the individual. It is unfortunate that reliable data on consumer Expenditure is not available in India ; but, some interesting studies can be made on the basis of such data as is available (vide Sankhya Vol. 20, Parts I and II) from the National Sample Survey. (The limitations of this data have been pointed out in Vol I, Ch. III, para 22). However, the following table gives some information for medical expenditure :—

Consumer Expenditure in "Medical"
(Per Person for 30 days)

(All-India : Rural and Urban)

Expenditure Classes per person per month (Rs.)	Average Expenditure per month (Rs.)	Percentage of total expenditure
0— 8	0.01	0.16
8—11	0.09	0.96
11—13	0.11	0.92
13—15	0.19	1.36
15—18	0.27	1.64
18—21	0.37	1.89
21—24	0.46	2.04
24—28	0.51	1.98
28—34	0.84	2.74
34—43	1.21	3.21
43—55	1.73	3.66
55 & above	3.90	4.68
all classes	0.43	2.29

Source : N.S.S. December 1955—May 1956.

8. Foreward to Health in Independent India (1957).

The above data can be converted into an index for facility of quick comparison by adopting the average expenditure per month for all classes as the basis for comparison and regarding it as equal to 100. The expenditure on medical facilities is then calculated as a percentage of it and expressed in the form of an index-number showing the increase taking place with an increase in level of total expenditure.

The following table gives some idea of the effect of rising levels of expenditure on specific expenditure on medical facilities :—

Index Number of Consumer Expenditure
(Per person for 30 days : All India—Rural and Urban)
(Medical)

Expenditure classes per person per month (Rs)	Average Expenditure per month (Rs.)	Percentage of total expenditure (Rs.)
(1)	(2)	(3)
0—8	2	7
8—11	21	42
11—13	26	40
13—15	44	59
15—18	63	72
18—21	86	83
21—24	107	89
24—28	119	86
28—34	195	120
34—43	281	140
43—55	402	160
55 & above	907	204
All classes	100	100

(Source : N.S.S data December 1955—May 1956)

Limitations of consumer Expenditure data based on information made available by the National Sample Survey are many, (See Vol. I, Ch. III para 22) and, it would be unwise to draw any firm conclusions from such data as errors (of sampling) may vitiate any refined comparisons. However, the table does bring about that expenditure in the top group is very high in the case of medical expenses so that "medical care would seem to be the highest luxury in India which only the richer people can afford."

8·11 *The Third Plan.* Considerable increases in outlays on health programmes have been undertaken for the third plan. As against outlays of Rs. 140 and Rs. 225 crores in the First and Second Plans respectively, programmes in the Third Plan involve a total outlay of obout Rs. 342 crores; about Rs. 297 crores being in the States * and the rest at the centre. To quote from the Third Five Year Plan:—

"The broad objective of the health and family programmes in The Third Plan is to expand health services, to bring about progressive improvement in the health of the people by ensuring a certain minimum of physical well-being and to create conditions favourable to greater efficiency and productivity. Increased emphasis will be laid on preventive public health services."

9. The States and Social Services.

9·1 As has been pointed out earlier, the Constitution of India demarcates the functions between the Union and the States in such a way as to impose on the States the major burden of maintaining the social services. The emergence of a centrally conceived plan, however, led considerable assistance being provided from the Centre for developmental activities to the States. Further, a distinction between Plan and non-Plan expenditure gradually emerged which was, in essence, a distinction to demarcate between expenditure on schemes included in a given plan period and other expenditure not so included. It is obvious that the distinction is both artificial and based on accountancy concepts rather than on any scientific functional distinction for in a given year some expenditure on (say) education would be treated as Plan expenditure while other expenditure on education itself would be treated as non-plan. In short, the plan expenditure of one period becomes non-plan expenditure in the subsequent plan period and is regarded as normal or committed or non-plan expenditure. Such a distinction, it is obvious, is hardly scientific for neither the character of the expenditure nor its economic or social effects are in the least modified by such a distinction.

9·2 It would, therefore, be more appropriate to demarcate public expenditure, as :

(a) Developmental, including therein—

(i) Education,
(ii) Medical and Public Health

*For Statewise details, See Vol. I, Ch. XI, Para 7.

(iii) Agriculture and rural development
(iv) Community Development
(v) Animal Husbandry and Cooperation
(vi) Irrigation and Cvil Works

and (b) Non-Developmental, including therein —

(i) Administrative expenditure including cost of collection of revenues.
(ii) Interest charges and Debt services
(iii) Miscellaneous and Extraordinary expenses.

The above classification is, of course, not exhaustive and would probably leave a sizeable chunk of expenditure not strictly to be included in any specified item. The intention of any grouping, however, should be to bring out the functional distinction *viz.*, whether the expenditure contributes directly to social welfare and economic development or is concerned with the more limited 'police' funct'ons of the State. Of course, to the extent that any public expenditure is necessary, it must contrilbute, directly or indirectly, to aggregate welfare for law and order is as necessary for the community as education or industrial development or roads and communication ; hence public expenditure must, as such, confer some common benefit for unless it is directed to achieve a public purpose it should not exist in a modern state. The classification between Developmental and non-Developmental expenditure would broadly bring out that the former directly contributes to social benefit and promotes economic development while the latter, though essential for the existence of the State, could be regarded as of secondary importance in a developmental economy.

9·3 In view of the important role of the States under the Indian Constitution for developmental expenditure, a state-wise analysis of the growth of expenditure in the States during the Second Plan period would be of interest. The two statements that follow indicate the growth of Developmental and Non-Developmental expenditure in the States.[10] It appears that about 56 percent of the total expenditure may be regarded as Developmental while the remaining 44 percent constitute Non-Developmental expenditure. As regards Developmental expenditure, states with

9. For a discussion of the classification of Public Expenditure See, Lutz Public Finance, Ch. III.
10. For a general analysis of Expenditure in the States See Vol. I, Ch. X.

STATEMENT—I (for para 9·3)

Total Developmental Expenditure in States during 1957-58 to 1960-61

(Rs. Lakhs)

	Andhra Pradesh	Assam	Bihar	Bombay	J. & K.	Keral	Madhya Pradesh	Madras	Mysore	Orissa	Punjab	Raja-sthan	U. P.	West Bengal	All States
	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
1957-58	3383	1687	3643	5501	431	1972	2786	3601	3668	1344	2063	1575	5437	3411	40502
(Index)	(100)	(100)	(100)	(100)	(100)	(100)	(100)	(100)	(100)	(100)	(100)	(100)	(100)	(100)	(100)
1958-59	4269	1715	3081	6059	505	2421	3082	4027	4096	1453	2431	2003	5747	3533	44422
(Index)	(111)	(102)	(85)	(110)	(115)	(123)	(111)	(107)	(111)	(108)	(118)	(127)	(107)	(103)	(110)
1959-60	5142	2004	3807	7507	665	2780	3247	4962	4617	1702	2315	2281	6012	4174	51215
(Index)	(152)	(119)	(105)	(137)	(175)	(141)	(116)	(138)	(126)	(127)	(112)	(145)	(112)	(122)	(126)
1960-61	5127	2305	4118	8939	666	3223	3830	5302	5451	2047	2815	2595	6924	4531	57873
(Index)	(151)	(137)	(113)	(162)	(176)	(163)	(137)	(147)	(149)	(152)	(145)	(180)	(129)	(135)	(143)
Total 4 years	17921	7711	14649	28006	2267	10396	12945	17892	17832	6546	9624	8454	24120	15649	194012
(Percentage to All States)	(9·2)	(4·0)	(7·5)	(14·4)	(1·2)	(5·4)	(6·7)	(9·2)	(9·2)	(3·4)	(5·0)	(4·3)	(12·4)	(8·1)	(100·0)

STATEMENT—II (for para 9·3)

Total Non-developmental Expenditure in States during 1957-58 to 1960-61

(Rs. Lakhs)

	Andhra Pradesh	Assam	Bihar	Bombay	J. & K.	Kerala	Madhya Pradesh	Madras	Mysore	Orissa	Punjab	Raja-sthan	U. P.	West Bengal	All States
	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
1957-58	2128	1155	2326	6127	312	994	2259	2314	1643	1004	1571	1557	4506	3607	31503
(Index)	(100)	(100)	(100)	(100)	(100)	(100)	(100)	(100)	(100)	(100)	(100)	(100)	(100)	(100)	(100)
1958-59	2073	1163	3079	6768	408	1141	2409	2808	1802	1134	1786	1592	5867	4403	36433
(Index)	(121)	(101)	(132)	(111)	(131)	(115)	(107)	(129)	(111)	(100)	(130)	(103)	(128)	(122)	(116)
1959-60	2321	1376	3105	7415	475	1313	2629	3096	2080	1170	2414	1762	6804	4414	40374
(Index)	(109)	(119)	(133)	(121)	(152)	(132)	(117)	(133)	(128)	(123)	(171)	(115)	(149)	(123)	(128)
1960-61	3484	1761	3010	8340	484	1378	2779	3645	2502	1619	3595	1941	7203	4551	46292
(Index)	(164)	(152)	(129)	(136)	(133)	(139)	(123)	(157)	(140)	(161)	(240)	(115)	(157)	(126)	(147)
Total 4 years	10006	5455	11520	28650	1679	4826	10076	11863	8027	4927	9366	6852	24380	16975	154602
(Percentage to All States)	(6·5)	(3·5)	(7·5)	(18·5)	(1·1)	(3·1)	(6·5)	(7·7)	(5·2)	(3·2)	(6·0)	(4:4)	(15·8)	(11·0)	(100·0)

smaller budgets, as is to be expected, had a faster rate of growth. For instance, while Rajasthan and Jammu & Kashmir have recorded a rise of 80 percent and 176 percent respectively in 1960-61 over that of the base year, the performance of Kerala and Orissa with their indexes at 163 and 152 are much above the average. On the other hand; Bihar, Uttar Pradesh and West Bengal have a low rate of growth as also Bombay *i.e.* Gujarat and Maharashtra taken together.

9·4·1. In view of the special importance of education and Medical and Public Health in India, two special Tables showing the growth of expenditure on these two items are given on page 51 and 52. It will be seen that under education, growth has been faster in Rajasthan, Andhra Pradesh and Madras than in other states. However, strangely enough in Uttar Pradesh the increase has been as low as 23 percent compared to the average of 50 percent.

9·4·2. Under Medical and Public Health, the most significant rises are in Orissa, J & K and Punjab, while that of Bihar is unusually low. It is unfortunate that state-wise estimates of expectation of life are not easy to construct for it would have been interesting to analyse how far growth of expenditure in this category has contributed to improvement in expectation of life.

10. Central *versus* State Control of Social Expenditure

10·1 Expenditure by government—Union or State—must of necessity follow the distribution of functions between the two as laid down in the Constitution. In a planned economy, however, the concept of economy and efficiency in public expenditure is more important than a narrow legalistic approach on the basis of relative power and authority.[11] It has been pointed out earlier "that no modern State can permit wide disparities in the levels of social services in the different parts of the country, and that it must be the function of the national government to ensure adequate development of such services, especially those that have a nation-building character like education or public health. It is necessary to steer clear between undue encroachment into fields that are essentially local in their character and a lopsided development with pockets of inadequately looked after population; in short, a successful federal arrangement must secure allround development without curbing the autonomy of the States. It is necessary to recognise that there is no ideal scheme according

11. See Vol I, Ch. VIII.

STATEMENT—I (for para 9·4·1)

Education

(Rs. Lakhs)

	Andhra Pradesh	Assam	Bihar	Bombay	J. & K.	Kerala	Madhya Pradesh	Madras	Mysore	Orissa	Punjab	Raja-sthan	U. P.	West Bengal	All States
	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
1957-58	1037	450	824	2361	120	997	1034	1116	900	312	667	607	1445	1138	13038
Index	[100]	[100]	[100]	[100]	[100]	[100]	[100]	[100]	[100]	[100]	[100]	[100]	[100]	[100]	[100]
1958-59	1257	517	939	2476	135	1317	1112	1222	965	335	858	738	1561	1294	14726
Index	[121]	[115]	[113]	[104]	[113]	[132]	[107]	[109]	[107]	[107]	[123]	[121]	[108]	[113]	[113]
1959-60	1530	605	1143	2788	177	1475	1247	1515	1085	407	962	883	1678	1595	17090
Index	[148]	[134]	[138]	[118]	[147]	[147]	[120]	[135]	[109]	[130]	[138]	[145]	[116]	[140]	[131]
1960-61	1738	698	1325	3379	189	1617	1433	1839	1247	433	1125	1051	1780	1670	19524
Index	[164]	[155]	[160]	[143]	[157]	[162]	[138]	[164]	[139]	[138]	[161]	[173]	[123]	[146]	[150]
Total 4 years	5592	2270	4231	11004	621	5406	4826	5692	4197	1487	3642	3279	6464	5697	64378
Persentage to All States	[8·6]	[3·5]	[6·6]	[17·1]	[1·0]	[8·4]	[7·5]	[8·8]	[6·5]	[2·3]	[5·7]	[5·1]	[10·0]	[8·9]	[100·0]

STATEMENT—II (for para 9·4·2)

Medical & Public Health

(Rs. Lakhs)

	Andhra Pradesh	Assam	Bihar	Bombay	J. & K.	Kerala	Madhya Pradesh	Madras	Mysore	Orissa	Punjab	Raja-sthan	U. P.	West Bengal	All States
	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
1957-58	424	185	460	884	55	256	338	460	307	139	234	259	545	611	5157
Index	[100]	[100]	[100]	[100]	[100]	[100]	[100]	[100]	[100]	[100]	[100]	[100]	[100]	[100]	[100]
1958-59	466	217	515	892	61	335	433	527	342	158	289	349	578	624	5786
Index	[109]	[117]	[112]	[101]	[110]	[130]	[128]	[114]	[111]	[113]	[123]	[134]	[106]	[102]	[112]
1959-60	548	302	584	1116	73	400	434	683	371	191	337	436	640	783	6898
Index	[129]	[163]	[127]	[126]	[132]	[156]	[128]	[148]	[120]	[137]	[144]	[168]	[117]	[128]	[134]
1960-61	727	294	566	1208	102	445	557	714	463	259	421	450	751	867	7824
Index	[171]	[158]	[123]	[136]	[185]	[173]	[164]	[155]	[150]	[186]	[179]	[173]	[137]	[142]	[152]
Total 4 years	2165	998	2125	4100	291	1436	1762	2384	1483	747	1281	1494	2514	2885	25665
Percentage to All States	[8·4]	[3·9]	[8·3]	[16·0]	[1·1]	[5·6]	[6·9]	[9·3]	[5·8]	[2·9]	[5·0]	[5·8]	[9·8]	[11·2]	[100·0]

to which a distribution of functions, and hence of expenditure, may be effected between the Union and State Governments, especially in India where the States are more geographical and cultural units than economic ones. It is the relative efficiency, in the sense of net welfare added, of the two types of administrative agency which is important and, in any assessment of the economic effects of public expenditure one must recognise both its direct and indirect benefits."

10·2 The Third Five Year Plan rightly recognises that public activities which improve the quality of the people and their social life are in effect productive and could be regarded as the highest form of investment of public funds. It has been stated that [12]:

> "Considerable emphasis is being given in the Third Plan to the development of education and other social services. In a scheme of development which relies heavily on public understanding and response and on cooperation and voluntary effort, the significance of these programmes cannot be too greatly stressed. They are essential for ensuring a fair balance between economic and social development and, equally, for realising the economic aims of the Plan."

The provision made in the Third Plan for Social Services does not seem to have recognised adequately the great significance of such services, for the provision, though higher in absolute amount, is a lower percentage of the total ; the provision for 'social services and miscellaneous' for the Third Plan is Rs. 1300 crores as compared to Rs. 830 crores in the Second Plan, the former being 17 percent of the total financial provision while the latter was 18 percent.[13]

10·3 Public Expenditure must in the long run be financed by Public Revenues, and in a sense there is no fundamental difference between raising the requisite funds either through taxation or through profits of public enterprises for both can be made as equitable (or inequitable) as public policy chooses to make it. It is, however, a fallacy to hold that expenditure on a project' is necessarily more likely to yield revenues than expenditure on education and public health for the latter may equally increase ability and desire to work and save, though obviously such

12. Third Five Year Plan P. 50.
13. Third Five Year Plan P. 58,

beneficial effects can come only after a suitable lapse of time. It has been said [14] that:—

> "There exists in the world of to-day a practically perfect correlation between the education level and the economic level in the various countries. This is so even if the measurements are simplified and qualified: The correlation between *literacy* and *national income* is astonishingly firm. The verdict will be the same even though not the statics but the dynamics of a national situation are judged: rise of educational level and increase in the rate of economic growth proceed together."

The same indeed could be said of the health of the people; no country with a high death rate as India has can hope to achieve progress.

14. Mrs. Alva Myrdal, Problems in the Third Plan, P.184.

II

COMMUNITY DEVELOPMENT

1. Introduction.

1·1 The Constitution of India envisaged the goal of the Indian people as a welfare State in which the individual will live for the Community and the Community for the individual. Planning in India has for its basic objective the reducing of inequalities in income and wealth, and the securing of a more even distribution of economic power. As the Third Five Year Plan asserts

> "The problem of reducing disparities in income and wealth is, in part, one of correcting existing inequalities, but its more important aspect is represented by the need to create conditions under which rapid growth can be achieved alongside a marked reduction in economic and social inequalities."

1·2 The extension of welfare activities of voluntary social service organisations go a long way to create the preconditions for equality of opportunity within the community. In the context of a Welfare State the community development movement has an important role to play, and is required to place greater emphasis on measures to raise the levels of living and to provide work opportunities for the less privileged sections. Succinctly stated "The purpose of the Community Project shall be to serve as a pilot in the establishment, for the men, women and children covered by the project area, of the 'Right to Live'. In more specific terms, the objective of the Community Development and National Extension programme is to assist each village in planning and carrying out an integrated, multiphased family and village plan directed towards self-improvement in all the facets of individual and community life."

1·3 The Community development programme has, since its inception eight years ago, is expected by October

1963 to extend over the entire country. At the end of the Third Plan about 2,100 blocks will be in their first stage, about 2000 in the second stage and over 1000 blocks will have completed 10 years of developmental activity, and, the provision under the third five year plan under community development and co-operation provides a total outlay of Rs. 400 crores. The table given below indicates an analysis of the State-wise coverage of the programme :

TABLE for 1.3

Coverage of the Programme according to States

States	No. of Blocks into which delimited	Blocks allotted upto 2nd October, 1960 No. of Stage I Blocks*	No. of Stage II Blocks	Total (3) & (4)	Villages covered by Stage I & II Blocks ('00 No.)	Population covered by Stage I & II Blocks (lakh Nos.)	No. of pre-extension Blocks
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Andhra Pradesh	445	192	89	281	193	188	44
Assam	162	57	27	84	141	46	12
Bihar	575	248	107	355	460	237	58
Gujarat	224	83½	46	129½	110**	86	20½
Jammu & Kashmir	52	38	14	52	59	23	...
Kerala	142	55	32	87	31**	78	14
Madhya Pradesh	416	154	108	262	484	161	36
Madras	375	131	80	211	121	159	32
Maharashtra	425	153	85	238	243	157	46½
Mysore	268	107	57	164	181	109	24
Orissa	307	127	49	176	271**	116	32
Punjab	228	93	60	153	140**	104	18
Rajasthan	232	85	54	139	205	90	20
Uttar Pradesh	899	344	174	518	699	335	92
West Bengal	341	123	50	173	227	120	34
Union Territories	133	50½	37	87½	117**	31	7
Total	5224	2041†	1069	3110	3682	2039	490

* Includes C.D. and Multipurpose blocks.

** Estimated.

† Marginal adjustments within this ceiling are possible.

2·1 The programme of community development is not merely an integrated programme but must be viewed as an integral part of a programme for improving all aspects of rural life and, above all, for establishing a sound economic base through rapid agricultural development. While progress of expenditure under various sectors of the programme may be some guide, its success or otherwise is neither a matter entirely of financial volumes nor of figures of physical targets and achievements. However, some objective idea can be got from the growth of government expenditure under various sectors of the programme indicated below :

TABLE for 2·1

Government Expenditure Under Various Sectors of the Programme (Rs. lakhs)

Item	Durnig Second Plan						During First Plan	Total (7) Plus (8)
	1960-61* April-60 to Sept 60	1959-60	1958-59	1957-58	1956-57	Total		
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
Block Head-quarters (incl. Transport, Office-building, Eqpt. etc.)	565	1232	1220	1033	735	4785	1051	5836
Agriculture and Animal Husbandry	72	263	222	129	125	811	355	1166
Irrigation and Reclamation	262	1035	1145	789	457	3688	1083	4771
Health and Rural Sanitation	114	352	336	269	232	1303	379	1682
Education	69	260	255	220	193	997	344	1341
Social Education	54	239	215	151	102	761	200	961
Communication	70	251	230	203	222	976	516	1492
Village Industries	71	171	104	80	86	512	218	730
Housing	76	205	207	190	169	847	173	1020
Unclassified (incl. imported equipment, suspense charge etc.)	70	244	79	66	57	516	279	795
Total	1423	4252	4013	3130	2378	15196	4598	19794

Partially revised figures upto 1958-59 and provisional figures for 1959-60. * Figures for J & K, Madras, U.P., Manipur and N.H.T.A. are upto June, 60.

2.2. Figures of state-wise government expenditure are indicated below :

TABLE for 2.2

Government Expenditure according to States

(Rs. lakhs)

States	1960-61 April, 60 to Sept, 60	During Second Plan 1959-60	1958-59	1957-58	1956-57	Total	During first Plan	Tota (7) plus (8)
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
Andhra Pradesh	190	342	321	296	176	1325	286	1611
Assam	39	94	144	114	116	507	229	736
Bihar	298	506	518	344	225	891	367	2258
Bombay :								
(i) Gujarat	104	747	691	417	291	2461	595	3056
(ii) Maharashtra	211							
Jammu & Kashmir	7*	76	54	62	16	215	31	246
Kerala	42	117	67	55	86	367	92	459
Madhya Pradesh	108	318	373	394	286	1479	521	2000
Madras	48*	295	200	192	161	896	283	1179
Mysore	94	244	203	148	86	775	73	848
Orissa	N.A.	222	223	148	141	734	209	943
Punjab	52	172	173	153	86	636	458	4094
Rajasthan	64	209	244	185	159	861	214	4075
Uttar Pradesh	72*	647	539	425	329	2012	857	2869
West Bengal	68	154	177	136	166	701	247	948
Union Territories	26*	109	86	61	54	336	136	472
Total	1423	4252	4013	3130	2378	15196	4598	19794

Partially revised figures upto 1958-59 and provisional figures for 1959-60.

*Figures for J & K, Madras, Uttar Pradesh, Manipur and N.H.T.A. are upto June' 60.

3.1 Considerable amounts are sanctioned as grants-in-aid, and two statements are given below indicating grants-in-aid statewise for

(a) Plan Schemes

(b) Non-plan Schemes,

STATEMENT I

(Statement for para 3.1) Statement showing amounts of grants-in-aid sanctioned to States for the C.D. programme since the beginning of the Second Five Year Plan (Plan schemes)

(In lakhs of Rs.)

State	1956-57	1957-58	1958-59	1959-60	1960-61
Andhra Pradesh	97·19	82·89	91·97	176·00	147·27
Assam	20·21	53·62	33·73	36·98	48·91
Bihar	88·68	109·21	112·53	185·89	211·87
Bombay	98·76	67·52	140·49	227·32	187·70*
Jammu & Kashmir	24·11	15·93	14·92	30·89	33·00
Kerala	27·20	14·06	29·59	34·84	46·80
Madhya Pradesh	111·49	104·86	104·79	129·09	147·90
Madras	92·98	68·71	66·41	102·68	122·81
Mysore	27·95	21·84	60·84	79·18	96·63
Orissa	50·17	46·28	72·76	118·75	103·01
Punjab	49·13	58·52	61·63	77·62	82·90
Rajasthan	55·87	56·54	54·58	67·61	78·68
Uttar Pradesh	127·73	181·30	227·30	254·31	282·58
West Bengal	42·47	43·41	61·16	91·74	104·75
Total	913·94	924·69	1132·70	1612·90	1694·81

* Rs. 71·20 lakhs for Gujarat and Rs. 116·50 lakhs for Maharashtra.

STATEMENT 2

(Statement for para 3.1) Statement showing amount of grants-in-aid sanctioned to States for the Community Development Programme since the beginning of the second Five Year Plan.

Non-Plan Scheme'

(Rs. lakhs)

State	1956-57	1957-58	1958-59	1959-60	1960-61
Andhra Pradesh	...	4·29	9·99	13·88	23·43
Assam	...	0·99	3·47	3·05	7·09
Bihar	...	4·29	8·01	18·32	30·60
Bombay	...	...	10·95	13·22	31·35*
Jammu & Kashmir	...	0·45	0·93	2·54	4·78
Kerala	...	1·23	6·17	3·98	8·25
Madhya Pradesh	...	6·43	16·75	19·14	26·32
Madras	...	2·81	8·26	13·16	18·89
Mysore	...	...	0·46	...	13·36
Orissa	...	1·24	5·21	10·08	14·58
Punjab	...	3·54	6·54	10·44	15·75
Rajasthan	...	...	7·67	9·65	13·94
Uttar Pradesh	...	2·26	8·79	26·70	49·83
West Bengal	...	0·91	6·13	29·47	15·67
Total	...	28·44	99·33	153·63	273·94

* Rs. 11·10 lakhs for Gujarat and Rs. 20·25 lakhs for Maharashtra.

3·2 Since much emphasis is laid on the concept of people's contribution in the Community Development programme, a statement is given below indicating the growth of this contribution, for if the movement is really to succeed it must convert itself from a Government's programme with people's participation to a people's programme with Government's participation.

STATEMENT (for para 3·2)

People's Contribution according to States.

(Rs. lakhs)

States	During Second Plan 1960-61 April' 60 to Sept' 60	1959-60	1958-59	1957-58	1956-57	Total	During First Plan	Total (7) Plus (8)
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
Andhra Pradesh	34	69	129	130	137	499	149	648
Assam	8	33	20	16	43	120	116	236
Bihar	147	346	350	210	207	1260	318	1578
Bombay :								
(i) Gujarat	19	29*	111	112	144	519	257	776
(ii) Maharashtra	31	73						
Jammu & Kashmir	N·A.	N.A.	11	9	1	21	7	28
Kerala	9	17	30	35	31	122	38	160
Madhya Pradesh	30	103	127	152	84	496	167	663
Madras	25	72	76	71	31	275	93	368
Mysore	13	34	31	46	48	172	83	255
Orissa	N.A.	29	23	21	22	95	47	142
Punjab	55**	157	182	184	83	661	420	1081
Rajasthan	35	46	156	117	167	521	142	663
Uttar Pradesh	64†	314	286	460	558	1682	559	2241
West Bengal	19	52	99	39	43	252	54	306
Union Territories	9	41	53	28	33	164	63	227
Total	498	1415	1684	1630	1632	6859	2513	9372

N.A. = Not available.

* Information for nine months – April to December, 1959.

** Provisional.

† Information for one quarter – April to June, 1960.

4·1 In the context of rebuilding the rural economy, especially the food problem, the basic problem in India is the organisation of the agricultural effort at the village level. In fact so great is the importance of this aspect, that the Third Five Year Plan lays down

> "The growth of agricultural production is of such critical importance that the principal test for the Community Development Movement at the present juncture must be its practical effectiveness as an agricultural extension agency."

4·2 The priority for agriculture is expected to be achieved by

(i) increasing financial provision for agriculture in the schematic budget of the Community development blocks,

(ii) the Agricultural Departments placing at the disposal of the Community development organisation at the block level the supplies, trained manpower and other resources needed,

(iii) the village level workers giving primary attention in the field of agriculture.

4·3 Adequate attention has to be paid in community development programme to provide adequately for the less-privileged sections of the village community so that the resources of the movement could be put more and more in the direction of assisting the less-privileged sections.

5·1 In the two tables given below an attempt has been made to illustrate

(a) the inter relationship in the Central budget between its total expenditure and its expenditure both direct and in the form of grants to the States for community development work ; and

(b) the expenditure of the States taken as a whole on Community Development in relation to its expenditure met from grants received from the Centre.

TABLE I (for 5.1)

Community Development Schemes

Central Government Revenue Expenditure 1955-56—1960-61

(Rs. lakhs)

	1955-56	1956-57	1957-58	1958-59	1959-60 RE	1960-61 BE
I. Centre's Expenditure on schemes of Community Developments, NES and Local development works.	9,69	9,28	10,86	13,85	19,93	23,22
II. Central Grants to States.	9,86	8,24	8,27	11,44	17,05	19,55
(a) Community Development	6,09	3,07	3,13	10,29	14,65	16,20
(b) N.E.S. Schemes	3,77	5,17	5,59	1,11	2,20	2,74
(c) Training Schemes	...	...	...	4	20	61
III. Total Expenditure of the Central Government	449,50	484,82	646,28	693,29	782,86	914,66
IV. Percentage of I to III	2.2	1.9	1.7	1.9	2.5	2.6

TABLE II (for 5.1)

State Governments Revenue Expenditure

I. Expenditure on Schemes of Community Development, N.E.S. and Local Development Works	26,89	27,80	31,69	39,06	40,96	51,92
II. Grants Received from Centre	9,86	8,24	8,72	11,44	17,05	19,55
III. II as % of I	36.6	29.6	27.5	29.3	41.6	37.6

5·2 It will be seen that while the Centre's expenditure on Community Development as a proportion of its total expenditure is an insignificant average of about 2%, the dependence of the states for this expenditure on Central grants is considerable and appears to be almost as much as 1 3rd on an average.

6.1 A steady progresssive emphasis on using democratic institutions at the district and block levels, in addition to panchayats which function at the village level is noticeable. It is true that in India, village panchayats are not a new idea but are perhaps as old as the earliest conception of organised community living. However, during the British regime the panchayats lost their significance for the administrative system developed continuously a reliance on the Civil Service and divested the panchayats of their executive and judicial functions With the advent of Independence, a new orientation of outlook took place and a revival of the panchayats started. The constitution of India recognised the importance of the panchayats as the basic unit of democracy at the village level and has laid down in Article 40 that "The State shall take steps to organise village panchayats and endow them with such powers and authority as may be necessary to enable them to function as units of self-government"

6·2 Revival of panchayats are being undertaken with a view to enabling them to play their appropriate role in bringing about rural development, and, various States have recently enacted new Panchayat legislation or amended their old ones to bring them in line with modern thinking. Bombay, Jammu and Kashmir and Madras enacted new legislation in 1958, followed by Assam and Mysore, in 1959. West Bengal, Punjab, Bihar and Delhi amended their respective Acts in 1959 and Rajasthan in 1960.

6 3 The entire trend of democratic decentralization is an expression of a national policy and is a part of the attempt to associate the people more intimately in nation building activity so as to give substance to the democratic ideal. The ideal is to achieve *Panchayati Raj* which envisages the transfer of the more significant developmental functions to self-governing institutions at various levels. The basic philosophy constitutes a faith that the village institutions being nearer to the people and being directly answerable to them would be able to reçognise more fully the needs and demands of the locality. It is necessary to recognise that a village without its own organizations and institutions can hardly think, plan or act as a village unit for it is only

through organised expression of wants and assertions of legitimate rights that any raising of the levels of living of the village people can take place. Any successful fruition of the community programme must make it a people's movement with the panchayat as the responsible motivating force at the village level.

7. Objectives of the Community Development and National Extension Programmes.

7.1 It is desirable to understand and appreciate that the Community Development and National Extension Service are not merely a scheme of welfare activity for the State nor also only "Just another department or Ministry of the Government of India"; it is an act of faith, a sort of a religion whose objective is the worship of man. It has been stated[15] :

> "Experiences in different parts of the world confirm that poverty can be eradicated and wealth created in its place. However, it remains yet to be proved that physical well-being for man can co-exist with the freedom and dignity of his spirit. Nowhere has individual freedom been prized more highly, nowhere has the lowliest of individuals been deified as was done in India through the proclamation 'every soul is potentially divine.' To risk this birth-right of man for an additional crumb of bread, a scrap of clothing and some space under a roof would be a negation of all that India stood for during the ages. Yet freedom and deification of the spirit mean little to one with an enforced hunch on the spine, with starving children by the side, with no defence against the weather. Should man barter his soul for these elementary needs of life? Democracy will not survive, if it cannot find a living answer to this basic question. Community Development in India is an all-out quest for this answer"

7.2 In specific terms the functions of the Community Development and National Extension programmes are :

(i) increasing agricultural production

(ii) improving existing village crafts and industries and organizing new ones

15. Shri S.K. Dey, Minister for Community Development and Co-operation.

(iii) providing minimum essential health services and improving health practices

(iv) providing required educational facilities for children and an adult education programme

(v) providing recreational facilities and programmes

(vi) improving housing and family living conditions

(vii) providing programmes for village women and youth.

The realisation of these objectives require the development of village leadership and the establishment of village institutions that are largely representative of village life. It requires economic upliftment through self-help and implies the raising of the incomes of the people. Above all, it requires "to develop the village people to become self-reliant, responsive citizens capable and willing to participate effectively and with knowledge and understanding in the building of our new Nation".

7.3 In the overall emphasis on village improvement, one may sometimes forget that aggregate welfare is a misleading concept unless it takes into account the necessity of the benefits of community development programmes reaching the less privileged sections of the village community in adequate measure. There is reason to believe that it has not done so ; though, it is reported that recently there has been a degree of improvement in this respect.[16] It is, perhaps, this lack of equitable distribution of its benefit that has led to a restricted development of people's response which was the primary objective of the community development programme. This has been frankly recognised in the Fourth Evaluation Report[17] as follows :—

> "The rural population in project areas is, generally speaking, now developing a feeling that Government is there not merely to rule but also to help. In fact, expectation of what Government can do to help has perhaps reached a stage beyond the current resources of Government. On the other hand, there has not taken place an equally strong sentiment of self-reliance and initiative, whether individual or co-operative."

7.4 *Integrated Rural Development.* Economic life in a village is not as individualistic nor as much subject to competitive forces as in urban areas. This is partly the result of a limited operation of the money-economy but

16. Third Five Year Plan, p. 342.

17. p. 20.

mainly the consequence of a greater impact of community-opinion on individual action which characterises village life. In a sense this is merely a more intimate adaptation of rural life to a socialist pattern of society where social values have greater significance. In such a background, where economic life is more intimately knit together, a co-ordinated development that brings together all the families in the village must constitute the appropriate approach. The programme of integrated rural development would involve :

(a) Every family having a plan,

(b) Every family having a link with the village co-operative society through direct membership of at least one adult member,

(c) Every family having an interest in the development of some activity which covers all members of the family, especially women and children,

(d) Every family being interested in general economic prosperity of the village with faith in complete absence of exploitation,

(e) Every family seeking to improve its own level of living not by depriving some other family but by enhancing the general level of living,

and, (f) Every family being associated, though *shramdan* of some sort, with some corporate activity of the village that gives community benefit.

The concept of an integrated rural development is not merely an economic plan but implies the recognition of a social purpose in planning which necessitates it being all-pervasive. It has been recognised[18] that "Without the rural economy as a whole growing rapidly enough, it is difficult to solve the problem either of the community in the village or of its weaker sections" ; but mere recognition without perceptible achievement perhaps does more harm than good. One must recognise that :

> "Shortfalls in social terms, that is, failure to put into effect social policies of radical intent, cause disbelief, cynism and even revulsion in the masses and among the professional people."[19]

8. Community Development—Evaluation and Assessment.

8.1. It is hoped that by October, 1963 the community development programme will extend over the entire rural

18. Third Five Year Plan Ch. XX, Para 15.

19. Gyan Chand, Social Purpose in Planning, article in Problems in the Third Plan, p. 83.

area of the country.[20] It already serves over 3,100 development blocks comprising about 370,000 villages. The total outlay on community development in the third plan is Rs. 294 crores with an additional provision of about Rs. 28 crores for *panchayats*, *i.e*, an aggregate of Rs. 322 crores in all, as compared to Rs. 240 crores in the first two plans. These indicate large investments and bold promises.

8.2. Programmes of community development are fundamentally different from other forms of rural reconstruction, for the essence of the programme lies in the aim that the people to be benefited are themselves to be enthused to undertake their share of the work voluntarily and in proper spirit. What, however, are the conditions[21] under which such development can produce lasting results ? It would appear that no permanent benefits can follow unless the following two conditions are satisfied :

(a) the area concerned has the ultimate productive capacity to raise its productivity sufficiently to be able to supply continuously the increased means necessary to maintain the higher standard of community living ; and,

(b) the programme of extension work is in harmony with the mind and culture of the people.

It is obvious that both these conditions are fundamental to the success of the programme. If (a) is not satisfied, no amount of enthusiasm will be able to maintain the artificially raised standard of living permanently without the 'block' becoming a liability of the State requiring subsidisation. Again, if (b) is not realised, no amount of added productive power will achieve any permanent results, for it would slowly and surely antagonize the people and take away the people's "participation" which is so essential to its success It seems that there is a sort of facile assumption that in every block both the conditions are always satisfied. In fact, the very concept of a uniform scheme of development for every area, irrespective of regional differences, is an indication of this assumption as per the decision* to adopt "a single scheme of community development which was spread over two stages, each of five years". No proper and full-fledged evaluation of the programme has yet been made ; the conclusions of the various evaluation reports of the Programme Evaluation Organization of the Planning

20. Third Five Year Plan, p. 332.
21. See Bose, S.K, article in Orissa Co-operative Journal, December, 1952.
* Third Five Year Plan, p. 333.

Commission are more of the nature of selective isolated studies than a complete effort to estimate the impact of the programmes on the people. It is, therefore, difficult to make a full appraisal of the results and achievements of the programme.

8.3 *The Balwantrai Mehta Study Team.* This was appointed in December, 1956. Its main purpose was to undertake a study of the efficiency and economy of the Community Project and National Extension Service Scheme The report of this team constitutes a landmark in the thinking on the subject and its recommendations have perhaps the greatest value because of its combination of idealism and realism. They held a very high opinion of the possibilities of the community project programme and stated :

> "While operating through the people's local organizations, the programme simultaneously strengthens the foundations of democracy on which our Constitution stands by making the villager understand the significance of development, and it makes him realise his position in this vast democracy. Thus, Community development and democracy progress through and strengthen each other. The community projects are of vital importance not so much for the material achievement that they would bring about but much more so, because they seem to build up the community and the individual and to make the latter the builder of his own village centres and of India in the larger sense".

The chief recommendations of the team are :

(i) Setting up of a body co-extensive with a development block for taking over the responsibility for developmental activities ;

(ii) establishment of a three-tier organization for simultaneous operation, *viz.*,

(a) the Village *Panchayat* at the base,

(b) the *Panchayat-Samiti* at the block level,

(c) the *Zila Parishad* at the district level ;

(iii) setting up of multi-purpose co-operative societies, working in close conjunction with local panchayats, in every village or for a group of small villages ;

(iv) shifting the emphasis from purely welfare activities to the more demanding aspects of economic development like rural industries, improvement of agriculture and animal husbandry etc.

(v) adoption of a continuing programme so as to ensure avoiding non-availability of funds at any stage,

(vi) greater acceptance of the schemes of State Governments without unnecessary further re-examination of details so as to achieve greater efficiency, economy and speed.

The Central Committee on Community Development approved in April, 1958 a revised programme more or less on the lines of the Balwantrai Mehta Team's suggestions. It was decided to replace the earlier three phases of National Extension Service, Community Development (Intensive) and the Post-Intensive Development by two stages of five years each, to be preceded by one year of pre-extension programme with greater emphasis on agriculture. It was also accepted that greater decentralisation in the development programme was desirable and that basically *Panchayati Raj* constituted the ultimate solution. Finally, a slowing down of the pace of expansion was accepted in view of the shortage of trained and suitable personnel.

8.4 *The U.N.T.T.A. Evaluation Mission.* A recent study of the working of Community Development Programme has been undertaken by the Mission appointed by the United Nations Technical Assistance Administration at the request of the Government of India. The Mission felt that for a programme like the one envisaged in India, an unjustifiably rapid rate of expansion was not desirable for "a rate of expansion that is unrealistic and to fast can only multiply existing difficulties and create illusory coverage achievements". In fact, they only drew pointed attention to a defect which is inherent in any system where efficiency of staff is judged by the evidence of numerical targets, especially of volume of expenditure. It has generally not been fully recognised that mere quantitative measurements are not enough, and, that in some cases, as for example in the case of new co-operative societies to be started, the very fixation of a target may be a dangerous beginning. So far as measurement of achievement in financial terms is concerned, one is aware of the distinction between 'audit of expenditure' and 'audit of performance', and for a community development programme it is the basic results realised that are often the better criterion than amount of expenditure undertaken*. Again, one is often apt to confuse a physical

* As Registrar, Co-operative Societies, Orissa, I invariably judged Assistant Registrars not so much by loans disbursed but by overdues collected without liquidation or supercession proceedings.

achievement with the basic result *viz.*, re orienting the villager. It is necessary to emphasise that achievements do not lie in so many miles of roads built, or in so many wells dug, or even in so many extra tons of production raised, but in whether the people have demanded these essentials of a higher level of living and done them on their own initiative. If it was merely the results that one should look at, a special programme of Community Development was not necessary; it could have been achieved more cheaply and more efficiently by a paternal State working through a team of impersonally efficient civil servants. In fact, the most serious condemnation of the Community Development Programme is to be found in the Seventh (1960) Evaluation Report when it says:

> "......One gathers the impression of an inadequately co-ordinated endeavour, Governmental rather than popular in character, and sustained more by hope than achievement".

The Mission recognised the necessity of divorcing the programme from the preoccupation with expenditure achieve ments and so suggested the adoption of some scheme whereby State subsidies or grants were linked to potential economic return. Finally, the Mission emphasised the need to move away from the past emphasis on amenities rather than production and suggested greater efforts on agricultural improvement, specially increased food production.

9. The Future.

The statistician cannot evaluate Community Development; he cannot do so simply because it is not a programme of physical or financial targets. In fact, what may appear as a thumping success may indeed be the greatest failure if it was achieved through compulsion or through tempting government subsidies. To quote Dr. Douglas Ensminger:[22]

> "The Community Programme was created to awaken the village people from mental inertia, and to help them realize that through exerted self-effort and self-help they can achieve the fruits of freedom, greater economic security and social justice. Any evaluation and critical analysis of the Community Development and National Extension block programmes must, therefore, start with an acceptance of the basic objective of the programme as being the building of a significant village culture, using culture in the broadest sense of the word as a *pattern of society*."

Obviously this cannot be done sitting in ivory towers and issuing directives and circulars nor by merely a large budget demand.

22. A Guide to Community Development p. 197.

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III

RURAL INDEBTEDNESS AND THE CREDIT NEEDS ON AGRICULTURE

1. Agricultural Indebtedness—the Concept.

1·1 The economic condition of the agriculturist in India has never been very prosperous and till practically the beginning of the Second Plan period, he was, perhaps, the one economic group for whom it would not have been wrong to say that he laboured "not for profits, not for a net return, but for subsistence." It was only after 1955-56, that a certain measure of prosperity came to the agriculturist, and, he began to have some choice in the matter of how much of his produce he would sell and how he would raise his level of living* by increasing the retention ratio of his produce. In a sense, borrowings by the cultivator in the past were unavoidable, that is he had no option but to take recourse to borrowing for his very existence was at stake. There was considerable truth in the remarks made in the Report of the Royal Commission on Agriculture[23] that :

> "When his land has passed into the hands of his creditor, no legislation will serve his need; no tenancy law will protect him, for food he needs land and for land he must plead before a creditor to whom he probably owes more than the total value of the whole of his assets."

1·2 It is, however, necessary to recognise that borrowing as such cannot lead to indebtedness. To say that it is not borrowing but failure to repay that leads to indebtedness may sound fatuous, but it is only by understanding the fullest implication of the causes of failure to repay that we would be able to appreciate fully the causes of indebtedness for the reasons for failure to repay are quite distinct from

* The reader may acquint himsolf with this Question. See Vol. I, Ch. III.

23. p. 433.

those which led to the borrowing. An appreciation of this position would also enable us to recognise that mere control over borrowing is not a full solution of the problem of indebtedness as the latter can only be solved by increasing ability to repay. Indebtedness must be recognised as a condition of economic distress and distinguished from a condition of being in debt. Under modern conditions, the concept of not free from debt' has no meaning, for borrowing for purposes which lead to an increase of income creates its own means of repayment and has little bearing on the problem of indebtedness. It is necessary to bear in mind that every occasion for borrowing cannot be regarded as a cause of indebtedness. It is only when, as a result of borrowing, liabilities tend to bear a heavier burden on the assets does borrowing tend to become a cause of indebtedness. It is, of course, possible that some causes of borrowing may, by themselves, contribute to a condition of a heavier burden on asset, as for example, a completely unproductive debt like the one incurred for repaying an accumulated debt; but, to the extent that borrowing is a phase of credit rather than distress, it is an aspect of economic management and should raise rather than lower income-earning power. It is for this reason that a discussion of the purposes of borrowing is of vital importance for they alone can give us any indication as to whether borrowing leads to indebtedness or not.

2. Agricultural Finance *Vis a Vis* Industrial Finance.

2·1 Economists distinguish between :

(a) long period capital, and

(b) short period capital,

meaning by the former those needed to acquire agents of production which help in the productive process over a considerable length of time, and by the latter those required to assist in the production of a given quantity of output. It is obvious that to the individual cultivator owning his land, land is only an agent of production for which a price has to be paid; in short, it is a capital asset which must yield him a return, and, the supply of which is elastic to the individual. However, from the Society's point of view, land has been defined as "the original and indestructible powers of the soil", and is, therefore, on a different footing from ordinary capital-goods since no productive forces have to be diverted from other uses to produce it and its total supply for all uses taken together is inelastic both in the short and the long period, excepting to the limited extent that it can be increased by reclamation or adding to its productivity

The distinction between long-and short-period capital, however, is not sharp and clear cut; especially, in the context of agriculture where a particular investment, like fertilizer, applied for a given crop also benefits succeeding crops.

2·2 The characteristic features of agricultural finance are :—

(a) the persistent small scale organization of agriculture limits available credit to the credit of the owner and prevents recourse to raising capital by the device of forming a limited liability company and borrowing by share-floatation;

(b) the agricultist's need for finance is generally constant and is not affected quickly and substantially by changes in output, which themselves are far less elastic than output in manufacture;

(c) the agriculturist undertakes a process of production the prospects of which are difficult to anticipate and more difficult to acquint others, so that the normal impersonal machinery of credit which supplies the needs of industry, *viz*, the Commercial Banks, are hardly able to meet its requirements;

(d) the asset of the agriculturist is land itself which has been recognised as an unsuitable form of security for commercial banking because
   (i) it is not readily realizable,
   (ii) it is difficult to value,
   (iii) it is particularly subject to fluctnating prices;

(e) the agriculturist must carry the entirer isks of his productive operation himself for, unlike industry he cannot transfer a part of his prospective profits by inducing his lenders to share in his risks.

To sum up, "......in the very nature of things the agriculturist is often isolated and remote from the normal opportunities for obtaining credit. Compared with those of the manufacturer and the trader, his operations are complex, long in their cycle and subject to exceptional risks from weather and disease beyond the ordinary ups and downs of prices and wages which he suffers in common with industrialists. For the greater part of the year, and especially when he is most in need of credit, his capital is sunk in forms of wealth, difficult for any one but an expert to value and not readily chargeable as security for an advance, while his personal training and method of life are not such as to fit him to surmount these natural disadvantages and to establish that

position in the credit market to which his financial stability and high standard of probity generally entitle him."[24]

3. Purposes of borrowing.

3.1 Normally borrowing is an economic operation and excepting the spendthrift borrower, every borrower expects a debt to be self-repaying; or, in other words, borrowing is a part of the investment process whereby the income-earning capacity of the asset (in the case of the agriculturist, his land) is raised sufficiently to provide for repayment of the loan. The true characteristic of a productive loan is this ability to provide for its own repayment; and, while certain purposes of borrowing are *prima facie* productive, it is a mistake to regard every borrowing for such purposes as productive. Productiveness is a balancing of costs with additional yield and a high rate of interest could make an investment, which would otherwise have been productive, incapable of adding sufficiently to income to repay itself. It is, therefore, a fallacy to think of such distinctions as productive or unproductive borrowing in the abstract and relate them to types of purposes; one should assess costs and return of a borrowing operation before classifying a loan as productive or unproductive. Further, another common fallacy is to regard all lending by the 'moneylender' as contributing to indebtedness while lending by co-operative societies as a panacea for all evils. An excellent example of this fallacy is to be found in the following statement[25] :—

> "To stabilise the effects of the debt conciliation, there should be simultaneous efforts to restrict the operations of the money-lender through legislative measures as well as to organise institutional credit for the peasantry"

The obivous implication being that no growth of indebtedness is possible for loans taken from organised institutions, a statement which is highly questionable in view of the fairly high rates of interest which the ultimate borrower has to pay even for co-operative loans. Loans advanced by co-operative primary societies were at varied rates of interest ranging from 6¼% to 16% and, few who have any idea of the real profitability of Indian agriculture would accept that a 11% rate of interest can be paid along with repayment instalments from the increase in

24. Report of the Committee on Agricultural Credit in England.
25 Report of the Congress Agrarian Reforms Committee, p. 95.
26 There may, of course, be other good justification for such rates of interest, for cheap credit may not be the summum bonum of Co-operative Banking. See Bose, S. K., Article in Orissa Co-operative Journal December, 1954.

income following from the investment of the loan amount to the agricultural process.[26] It is, of course, no justification to argue that "Rates of interest charged by the Co-operatives in the different districts need to be studied in the context of the prevailing rates of interest charged by other agencies" (Vide., Rural Credit follow-up Survey, 1956-57, General Review Report p. 434), for the productiveness of a loan does not depend on the cost of borrowing from alternative agencies.

3.2 Credit requirements are a function of the nature of the economy under which the cultivator carries on his agricultural operations. In essence, the agricultural economy of India is a deficit economy which is characterised by the following features :

(a) levels of living hardly very much above subsistence level,

(b) use of stereotyped methods of cultivation,

(c) Pattern of expenditure typical of low-income groups with emphasis on primary requirements,

(d) small size of holdings so that the value of asset held in the form of land is low, and,

(e) restricted marketability of the limited marketable surplus available to the individual cultivator.

In an economic environment such as this, flow of credit can hardly be expected to follow normal economic channels, but a classification of the purposes of borrowing[27] may be useful for an understanding of the problem. The different types of finance required may be classified as follows :

I. Agricultural.

(i) Short term—	Purchase of seed. Payment of wages. Purchase of implements. Minor land improvements. Current farm expenses.
(ii) Medium and Long term—	Purchase of Livestock. Permanent improvements in land. Purchase of additional land. Purchase of mechanical aids.

II. Non-Agricultural.

(i) Short term—	Current non-farm business expenditure.

27. See Reserve Bank of India, Rural Credit Follow up Survey 1956-7, General Review Report p. 988, p. 57.

(ii) Medium and Long term— Non-farm business expenditure on Capital account.

III. Consumption.
Generally only Short-term— Medical expenses, Social ceremonies, Family expenses involving comparatively larger amounts.

IV. Repayment of old debt.

V. Other Expenses.

It is clear that only borrowing for purposes indicated under I above can come within the realm of productive borrowing in the economic sense of the term. It would, however, be unrealistic to assume that non-productive borrowing is always avoidable for economic distress or social conventions may often make such non-productive borrowing inescapable. In fact, sometimes the very necessity of continuing cultivation may require borrowing of an unproductive but necessary character like, for example, borrowing to prevent sale of land for non-repayment of ancestral debt.

4. Estimates of Indebtedness.

4·1 Estimates of the total volume of outstanding debt are difficult to make. The indebted person is generally reluctant to reveal his liablities accurately and when he does so with a view to obaining some benefit in the form of conciliation, or scaling down,he has a tendency to overstate, especially as he hardly ever keeps proper records while the records of his lending creditor, the village money-lender, are generally suspect. Further, the volume of outstanding debt is affected by a number of complex factors which make comparability over time of doubtful value. For example, with the growing commercialization of agriculture and with the extension of the monetized sector, borrowing for current as well as capital purposes tends to become more general and increase the money volume of outstanding debt. Again, the character of the agricultural season in the period preceding the estimation, or the trend of prices have important effects on the volume of estimated indebtedness. Finally, an increase in the volume of debt does not necessarily indicate an increase in the burden of indebtedness for unless the increased volume of debt has a larger component of unproductive debt, it might simply mean that development expenditure was being financed by borrowing and that it had not yet started to give the returns from which the outlay would be repaid. These

difficulties are especially great if a breakdown of the All-India estimates by States or regions are to be attempted for obviously, economic conditions being different in different areas, assumptions which are logically acceptable for one area may not be applicable for another area.

4·2 As far back as 1911, Sir Edward Maclagan observed :

> "It has long been recognised that indebtedness is no new thing in India. The writings of Munro, Elphinstone and others make it clear that there was much debt even at the beginning of our rule. But it is also acknowledged that the indebtedness has risen considerably during our rule and more especially during the last half century. The reports received from time to time and the evidence of annual sale and mortgage data show clearly there has been a very considerable increase of debt during the last half a century."

The following indicates some of the estimates made of total agricultural indebtedness in the country :

Year	Estimated indebtedness in Rs. Crores	Authority
1911	300	Sir E. Maclagan.
1925	600	M. L. Darling.
1931	900	Central Banking Enquiry Committee.
1935	1200	Prof. P.J. Thomas
1937	1800	Reserve Bank of India.

Unfortunately official estimates of all-India indebtedness have not been made in recent times. Even the estimates made by the Central Banking Enquiry Committee have been regarded as unreliable.[28] However, certain enquiries have been made from time to time in various States through enquiries, sometimes sponsored by State Governments and sometimes by individual scholars and research workers. It is difficult to construct any All-India estimate on the basis of such estimates for particular States, and it would be obviously not possible to hazard any opinion as to whether the total indebtedness in the country is on the increase or decrease, though the Rural Credit Follow-up Survey (1956-57) of the Reserve Bank of India concluded[29] that the data

28. Report of the Agricultural Finance Sub-Committee of the Government of India, p. 3.
29. General Review Report p. 73.

revealed 'the general trend of an increase in the volume of debt during the year covered by the investigation,' even though it recognised that factors affecting the increase in debt maybe widely different in different context so that it was :

> "………not possible to make comments in relation to the working of the economy, based on the data on increase in debt, in absolute terms or in relation to the debt at the beginning of the year."

4·3 Comparable estimates of rural indebtedness for the different states are not available. Even the few estimates that are available for particular States are not usable for comparative purposes because of differences in concepts, coverage etc. It is unfortunate that the National Sample Survey have frittered their energies in repeating collection of expenditure data from year to year and did not consider it desirable to concentrate even once in making an attempt to collect data on rural indebtedness. However, the Rural Credit Survey of the Reserve Bank of India undertook an inquiry in 1951-52 which provides some interesting statewise data and which, in comparison with earlier enquiries, provides some indication of change in the volume of indebtedness over a period of time. The comparability is limited due to the following factors* :

(a) reorganization of States in 1956,

(b) differences in comparison base-year,

(c) lack of uniformity in the size of the family from State to State,

(d) absence of information as to the productive and unproductive composition of the debt.

The information as given in the Survey Report[30] is as follows :

State	Debt per family (in Rs.) Earlier Enquiry	Debt per family (in Rs.) Rural Credit Survey	Percentage increase (+) Decrease (—) In debt per family	Percentage increase (+) Decrease (—) In proportion of indebted families
(1)	(2)	(3)	(4)	(5)
Assam	205	219	+27	—16
Bihar	282	291	— 6	+10

30. Vol 1, Part I p. 180.

* Note 1. Figures in column 2 are those of the Provincial Banking Enquiry Committee (1929)

2. Figures in column 3 relate to 1951-52 Survey by Reserve Bank of India

3. N.A. means Not Available for comparison

(1)	(2)	(3)	(4)	(5)
Bombay	324	345	N. A.	N. A.
Madras	194	483	N.A.	N.A.
Madhya Pradesh	227	226	— 9	+ 9
Orissa	73	90	+52	—20
Punjab	468	417	N.A.	N.A.
Uttar Pradesh	162	316	+54	—28
West Bengal	168	164	N.A.	N.A.

It is difficult to draw any definite conclusion from the above table except, perhaps, that there has been an increase in debt per family in every case, the only significant exception being Punjab. (Madhya Pradesh and West Bengal show minor marginal declines which may be ignored). This, of course, is of little significance for 1930 was a depression year while 1951 was a year of high prices, the wholesale Index of All commodities (Base 1952—53=100) being 120·0, which would be much higher if 1930 prices were taken as base. If account, however, is taken of the impact of the wartime (1939-42) boom and the better conditions of prosperity that followed it, the rise in the money-burden of indebtedness does indicate an alarming trend. As the Committee on Agricultural Finance(popularly known as the Gadgil Committee) stated :

> "It might be possible to hazard the opinion that the total indebtedness in terms of money stood in 1944 at a level lower than in 1939 ; but that, at a later date, forces were already in operation leading to an increase in the total amount of indebtedness."

This trend towards increase apparently has continued and it is unlikely that the total volume of indebtedness has declined in recent times. It is possible that the Mahalonobis Committee* on Income-distribution would make some data available, for in order to assess changes in the level of living of the rural population, it would obviously be necessary for the Committee to assess the changes, if any, in the volume of rural indebtedness. We must, in the absence of other information at present, await the enlightenment that the committee should provide.

5. Causes of Indebtedness.

5.1 We have seen that borrowing as such cannot be a cause of indebtedness ; hence, causes of borrowing cannot be

* See Vol. I, Ch. I, para. 2.3.

regarded as causes of indebtedness. While there is no doubt that a low income and a deadweight ancestral debt must make repayment of borrowings difficult, and consequently contribute to indebtedness, it would be unwise to concentrate on these above as the primary causes of indebtedness. It would also not be proper to hold the money-lender and his practices as being the basic cause of rural indebtedness, even though the high rates of interests and his malpractices (to the extent they exist) could contribute to the growth of such indebtedness. It, thus, seems to be an exaggeration to argue[31] :

> "The two largest single factors depleting the peasants income are the exploitation by the money-lender in his double capacity as the credit agency and the marketing agency of the village. The exploitation works like a double-edged sword—high rates of interest on the loans to the impoverished agriculturists and low rates for their products. So there is a vicious circle—extreme poverty forces the peasant into the clutches of the money-lender and the exploitation by the money-lender leaves him poorer and a less efficient producer than before which makes his income still less. Thus goes on this poverty spiral of the peasantry."

Again, it was fashionable for pre-independence writers to regard the cultivator himself as responsible for his misfortunes and to maintain that it was his ignorance and improvidence, his extravagance, his large family, his fatalistic attitude to life and his docile acceptance of an ancestral debt that brought about the mounting volume of rural indebtedness. These views have proved to be as unscientific as the other one for the cultivator in India is undoubtedly uneducated (for no fault of his own) but he is certainly not incapable of economically managing his affairs.

5.2 The chief causes of indebtedness may be broadly classified as follows :

(i) Those that have led to an increase in the credit of the agriculturist and thus provided greater opportunities for borrowing.

(ii) Those that are connected with the cultivation of land.

(iii) Those contributed by the character of the agriculturist himself.

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31 Report of the Congress Agrarian Reforms Committee, Ch. V, para 64,

(iv) Those that are connected with the money-lender and his practices.

(v) Those that flow from the terms of borrowing.

As is to be expected, the various groups of causes are not independent but are to some extent mutually interdependent. It is obvious, for instance, that an exorbitantly high rate of interest may convert a loan applied to a productive purpose to an uneconomic investment and contribute to indebtedness ; but the high rate of interest may be the result of lack of collateral security or may be the result of risky and uncertain prospects of a particular culti vation operation. Similarly, excessive unproductive borrowing for social expenditure may cause indebtedness, and may in turn force up the rate of interest if the total outstanding debt tends to impose a heavier burden on the assets of the cultivator which obviously has been, in recent times, acquiring higher values due to rise in land-prices. In fact, what the Royal Commission on Agriculture stated more than thirty years ago is still substantially true *viz.*, that no reliable evidence is even now available as to whether the total rural indebtedness bears a heavier or a lighter burden to the assets of the indebted population.

5.3 The maintenance of law and order, the defininga nd recording of rights in land, the rise in the value of the agriculturist's produce and the growth of transferable rights in land which has substantially risen in value, have all contributed to an enhancement of the credit of the landholder. The rising credit has provided both an opportunity and a temptation to larger borrowings, and, increased the possibilities of rising indebtedness for obviously the cultivator did not, perhaps even could not, restrict his increased borrowing to only productive investment ; and, it is elementary economics that even if the percentage of his unproductive borrowings to total borrowings remains constant, a rise in total borrowings must contribute to a rise in aggregate indebtedness. There was, unfortunately, no adequate growth of opportunities to invest safely and conveniently so that all additional surplus were directed towards the acquisition of land whose value soared up. The growth of absentee landlordism brought in a class of investors who attached a prestige value to the ownership of land and who, unless restrained by laws relating to the alienation of land, were anxious to lend money to the improvident cultivator and acquire his land through a crushing burden of indebtedness.

5.4 Agricultural operations are, by their very nature.

uncertain and subject to the vagaries of nature. It is true that with an increase in irrigated area, with better chemical manuring and with increased use of scientific rotation of crops, contour bunding, prevention of soil erosion etc., it has been possible to progressively reduce dependance on mother nature ; yet, even now, the net profitability of agriculture in India is still only marginal and it is only in good crop years that the cultivator can keep away from unproductive borrowing. To the natural and unavoidable evils of agriculture as such, are added in India the twin evils of sub-division and fragmentation of land which makes for uneconomic cultivation, reduces the return on land and, by lowering net income, contributes to the growth of indebtedness. While it has to be recognised that sub-division of land is consequent on the laws of inheritance, its increased intensity is the result of a growing pressure of population on land. The smallness in the size of holdings* has led to the emergence of uneconomic units of cultivation depressing per capita net income of the cultivating family, and the consequent distress has been made worse by the decline of the cottage industries and the loss of supplementary income from subsidiary occupation in the off season.

5.5 The Indian agriculturist is said to be 'born in debt, live in debt and die in debt', and, in extreme cases a cultivator may remain indebted even though he himself never borrows. This is because of the crushing burden of ancestral debt which, even when it is not a legal obligation, is regarded as a moral and religious one that eats into the cultivators income, sometimes forcin ghim to borrow to pay interest charges and a part of the outstanding capital. The cultivator's love for social ceremonies, the pressure of village customs compelling heavy expenditure on the occasion of births, marriages and deaths in the family and expenditure on excessive litigation bred by the decline of the 'Village elders' have also contributed to his improvident borrowing and mounting indebtedness.

5.6 The high rates of interest charged by the money-lender makes borrowing even for productive purposes uneconomic and since such loans, due to the excessive cost of it, do not provide for their own repayment through adequate increased income, they become contributory causes of indebtedness. It is, however, necessary to recognise that whatever the source of the loan the same consequences will follow if the rates of interest are higher than the net addition to productivity that takes place through the investment of

* See vol I, Ch. I paras 4-11.

the borrowed capital. Whether the rates of interest charged by the money-lender is, in fact, excessive in view of the risks taken by him and the service rendered by his method of work is a moot point in this connexion for so far as the contributing cause of indebtedness is concerned, it is the level of the rate, and not its justifiability or otherwise, that is important. In fairness to the money-lender it must be admitted that his high rates of interest are of the nature of an insurance against risk, for the realized rate of interest is often much less than the stipulated rate, and, that, in a sense, he was in the past at least an indispensable feature of Indian rural economy. Some questionable practices, like demanding advance interest, manipulation of accounts, insertion in written documents of sums considerably in excess of actual money lent, have often been ascribed to money-lenders and, if true, must have contributed to growth of rural indebtedness.

5.7 To sum up, the large volume of rural indebtedness in the country has not been the result of any single factor but has been brought about by a variety of causes. At the root of the evil is uneconomic and unproductive borrowing, often made inescapable by the absence of adequate institutional credit.[32] However, mere provision of cheap credit is no solution ; it may even amount to alleviating 'the misery of the ryot as an opiate relieves pain' for it will not cure the trouble from which the misery arises. There can be no permanent solution to the problem unless borrowing is made productive and economic. The table given below indicates the relative shares of different purposes of borrowing, and, would reveal that a large portion of total borrowing is *ipso facto* a contributory cause of indebtedness for it makes no addition to the cultivator's income Based on the data in the Rural Credit Survey*, we find the position as follows :

Purpose of borrowing	*Percentage to total*
1 Capital expenditure on farm	27·8
2. Current expenditure on farm	9·3
3. Non-farm business expenditure	6·6
4. Family expenditure	50·2
5. Other expenditure	5·7
6. More than one purpose	0·4
	(100)

32 Third Five Year Plan, Ch. XIII paras 8-9.
* p. 274.

Obviously an economy which results in more than 50% of the borrowing to be utilised for non-productive purposes can hardly expect the borrowing rural population to be free from indebtedness.

6. The State and Remedial Measures.

6.1 The problem of rural indebtedness has always been serious enough to engage the attention of the Government who have taken various measures—legislative and administrative—to deal with the problem. These measures may be grouped as follows :—

(i) Those aimed at removing the need for borrowing, particularly unproductive borrowing.

(ii) Those directed against the excess of credit and attempting to protect the assets of the agriculturist.

(iii) Those attacking directly the power of the money-lender and regulating his activities.

(iv) Those attempting to provide alternative sources of supply, especially through the development of institutional credit.

(v) Those raising the productivity of agriculture and making investment in land self-repaying.

6·2 It has been pointed out earlier that borrowing as such is not an evil ; but, when a large percentage of the borrowing is for consumption purposes, the possibilities of a mounting volume of indebtedness are great. Furtther, frequent borrowings are often necessitated because of the absence of a "net surplus" due to low productivity and high costs of cultivation. The rigidity of money demands on the cultivator may also contribute to the necessity of frequent borrowing, though, so far as the state is concerned, its demands on the agriculurists in the form of Land Revenue has risen far less than the rise in the money value of his product. Of course, the cultivator's cost of living has risen because of the rise of prices of commodities that he has to purchase so that he has less to spare for re-investment in his agricultural operation. To reduce the need for borrowing, it is necessary to

(a) increase the cultivator's net surplus over cost of cultivation,

(b) reduce his money obligations, and

(c) educate him to a way of life where a voidance of consumption borrowing takes place.

The State has attempted to achieve all these through various measures. It has sometimes reduced the effective burden of land revenue and made its payment convenient through greater elasticity in its administration and collection. Again, through proper irrigation facilities the fatalistic dependance on the vagaries of the monsoon have been sought to be reduced so that the average income of the cultivator over a given period is more steady and higher. Finally through improvements in communication and marketing, the agriculturist has been enabled to obtain a better price for his product and increase his net income. These attempts are being continued, and

> "Programmes of agricultural production lie at the base of the comprehensive approach to the reconstruction of the rural economy which is embodied in the Third Five Year Plan. Development of irrigation, from large as well as small works, soil conservation programmes and supplies of fertilisers, improved seed and credit, along with the provision of extension services reaching down to the village level, are measures undertaken directly to increase production."[33]

To the extent that these succeed, the need for borrowing must get less; and, to the extent the improvements envisaged bring about a rise in the agriculturists' income, avoidance of indebtedness must become easier. Growth of an enlightened leadership in the rural areas would pioneer progress in many directions, including, it is hoped, in the social conventions and habits of living of the village community; these changes along with widespread education can alone bring about a reversal of values that would make borrowing to spend for unproductive social display unnecessary, and thus provide a stable foundation for the avoidance of indebtedness.

6·3 Land constitutes practically the only creditworthy asset which the cultivator possesses and which the lender for unproductive purposes would generally accept. The rising land-values, together with absence of equally profitable avenues of alternative investments, led to a large volume of loans being given to the agriculturist on the security of his land. In view of the high prestige-value associated with the ownership of land, the money-lender was anxious to possess and own it himself, and, transference of ownership of land on almost an alarming scale took place leading to the twin evils of absentee landlordism and an agricultural prole-

33. Third Five Year Plan, p. 301.

tariat—a class of landless labourers who previously owned land and knew no occupation other than cultivation. The evil consequences of large scale transfer of land from cultivating owners to non-agriculturist money-lenders were recognised and the Punjab Land Alienation Act was passed in 1900. The Act intended to restrict credit on the mortgage of land and hoped that this would indirectly reduce borrowing. In effect, however, agriculturist money-lenders stepped into the breach and the subsequent period was marked by an increase, and not a decrease, in the volume of indebtedness. As many of these agriculturist money-lenders were not direct cultivators the problem of absentee landlordism with non-owning cultivators continued unabated, especially as along with loans on long mortgages of land frequent *benami* transactions began to take place. Amendments to the Punjab Land Alienation Act have sought to provide progressively for :

(a) limitation of the period of mortgages
(b) declaring *benami* transaction inoperative
(c) prohibition even to agriculturist money-lenders from purchasing land of their debtors within three years of the final settlement or repayment of the debt.

Following the lines of the Punjab Act, many other States have attempted to control alienation of agricultural land to non-agriculturists. Similar Acts have been brought into operation in Bombay, Hyderabad, Madhya Pradesh and some other States. It must, however, be admitted that as a measure for controlling indebtedness it has not achieved much success, though some beneficial social results do seem to have followed from restrictions on transfers of land to non-agriculturists.

6·4·1. The village money-lender has always been a significant institution in rural economy ; and, even though sometimes he has proved to be a 'dangerous necessity,' he has been, and still is, an inescapable necessity. It is still true that "......the money-lender is an indispensable feature of Indian rural economy. He is easily accessible. His methods of business are simple and elastic. He maintains a close personal contact with the borrower, often having hereditary relations with the family of the borrower. His local knowledge and experience and his presence on the spot enable him to accommodate persons without tangible assets and yet protect himself against losses." There is sometimes a presumption made that his significance as a source of credit supply has been on the decline. Such views are often the result of what may be regarded as wishful thinking based on the following trends :

(a) growth of co-operative credit,

(b) legislative control of the money-lender,

(c) expanded finance made available through recent community project developments,

(d) rising prices obtained by the cultivator contributing to reduced necessity for unproductive borrowing for consumption purposes.

The facts, however, belie the expectations. The Reserve Bank's Rural Credit Survey Report gives the following information :

	Credit Agency	Proportion of borrowing from each agency to the total borrowings of Cultivators
1.	Professional money-lenders	44·8
2.	Agricultural money-lenders	24·9
3.	Relatives	14·2
4.	Traders and Commission agents	5·5
5.	Landlords	1·5
6.	Government	3·3
7.	Co-operatives	3·1
8.	Commercial Banks	0·9
9.	Others	1·8
		(100)

The above figures bring out the domination of the money-lender in the field of rural credit supply. The follow up Survey confirmed these trends as it was found that the borrowings from private credit agencies, which was nearly 92 percent during the earlier survey ranged, in 1956-57 (May to April) from 49% to 99%, while the proportion of outstanding debt to these agencies to total debt was equally high. It would, therefore, be unwise to underestimate the significance of the money-lender in, even present day, rural economy.

6·4·2 Various measures have been passed from time to time attacking directly the power of the money-lender. These measures are intended to protect both the honest borrowers and the lenders. It has, however, to be recognised that no legislation can help if there is collusive evasion, and, as long as the need for borrowing exists, legislative control of the money-lender may merely have the effect of

withering away the sources of rural credit and raising its costs. The more important of these measures are :

(a) *The Deccan Agriculturist Relief Act of 1879*, which allowed the courts to go behind the contract and to modify it in favour of the borrower so as to reduce an oppressive rate of interest, to prevent sale of land unless specifically pledged and to restore the land to the culivator even when there was a sale deed between the two parties. The Act also attempted to ensure fair play for the borrowers by making it obligatory on creditors to furnish accounts and grant receipts.

(b) *The Usurious Loans Act of 1918*, amended in 1926 attempted to improve the legal position of the borrower in various ways. The Courts were empowered to reopen and examine all loan transactions and to determine fair rates of interest, though the Act itself did not define 'excessive' or 'unfair'. The Act, however, did attempt to provide guidance as to the considerations to be taken into account in fixing the rate of interest, and these included, *inter alia*, the risk taken by the creditor, the financial condition and the need of the borrower, other charges paid by the borrower. Opinion has varied as to the extent to which the Act has been effective. The Royal Commission on Agriculture held the view that the Act was practically a dead letter, but the Central Banking Enquiry Committee did not agree with this view and were of the opinion that "the Act is capable of being worked to the advantage of the debtors", though they were unwilling to statutorily fix a definite limit to the rate of interest. The Congress Agrarian Reforms Committee of 1948, however, reported as follows :

> "In the course of our tours we had occasion to examine peasants in representative zones of the different provinces. We can safely say that the laws for restricting the operations of the money-lender have completely failed."

It is difficult to believe that much reduction in the rates of lending has, in fact, taken place as a result of statutory regulation, for the follow-up Rural Credit Survey of 1957 reported fairly large borrowings at rates even higher than 50%.[34] The Survey Report also came to the following rather damaging conclusion :

> "The data also show that even in the districts with fairly well-developed and monetized economies, cultivators had to obtain a large proportion of their borrowings at rates which were significantly

34. See General Reivew Report Ch. 4, para 4.9.

> higher than those usually charged by institutional credit agencies. Barring exceptional situations, the incidence of the burden of interest was heavier on medium and small cultivators, especially the latter group, than on big and large cultivators."

The above conclusion would tend to show that not only has little success been achieved in regard to lowering of the rate of interest, but also that agricultural borrowing has yet not succeeded in freeing itself from its credit-worthy base for it is the cultivator with lower asset who still has to pay the higher rate of interest.

(c) *The Punjab Regulation of Accounts Act, 1930,* is simply an attempt to protect the debtor from manipulated accounts by prescribing forms of accounts, and insisting on the debtor being supplied with these regularly. It also laid down that principal and interest must be shown separately so as to enable easier assessment of rates of interest charged. Similar Acts have been passed by many States. It is clear that such provisions can be of effect only if regular surpervision is undertaken which is not possible in absence of proper licensing and registration of money-lenders.

(d) *The Punjab Relief of Indebtedness Act, 1934,* was an enactment for the reduction of excessive rates of interest by fixing the maximum rates of interest. The Act drew a distinction between secured and unsecured loans for purposes of rates of interest, fixing a maximum of interest rate for each category. It is obvious that without adequate alternative sources of credit supply, mere statutory fixation of rates of interest is bound to be ineffective. There are reasons to believe that this Act has had practically the same type of effects as wartime control-prices had on consumer goods.

(e) *The Punjab Registration of Money-lenders Act, 1938.* The question of having a system of registering and licensing money-lenders is a controversial question on which much can be said on either side. Is is generally believed that compulsory registration would reduce questionable practices and bring about more healthy relations between the borrowing agricultural population and the registered professional money-lender who would conduct his business on fair and economic lines. On the other hand, such schemes of compulsory registration could lead to the drying up of the source of credit and might involve providing special facilities for enabling recovery of loans granted under restricted conditions. In any case, whatever may be the theoretical considerations, in practice such a step could hardly be expected to succeed

as long as there is an unsatisfied demand for borrowing. It is doubtful whether laws requiring the money-lender to get himself registered and to take a license for carrying on his lending business has achieved any significant results ; nor, is it likely to achieve any material improvement in the position of the borrower unless effective alternative sources of supply of finance can be developed.

6·4·3 The severe fall in prices that followed the economic depression of 1929 increased the burden of debt so much that in many cases it was thought necessary to provide relief by drastic legal measures. In the Punjab, debt conciliation boards were set up under the Relief of Indebtedness Act, and, subsequently when it was realised that voluntary conciliations were not having much effect, more drastic measures like the Punjab Debtor's Protection Act, 1936 and the Punjab Restoration of Mortgaged Lands Act, 1938 were passed ; the former Act exempted ancestral property from attachment as also standing crops, while the latter Act provided for restoration of mortgaged lands on payment of nominal compensation. However, it is doubtful whether such measures have proved to be beneficial in the long run. A dispassionate study of the trends of borrowing during the last three decades seems to suggest that such measures which benefit individuals in one sector of the economy at the expense of other individuals in another sector of the economy generally recoil to the disadvantage of the former in the long run unless their economic dependance on the latter can be removed. One, therefore, finds it difficult to understand how a measure like, for instance, the Madras Debt Relief Act of 1938 which considered the loan as repaid if total payment by the debtor in interest or capital repayment equalled twice the original sum borrowed, could economically improve the long period position of the debtor unless the latter was freed for all times from the necessity of borrowing from the creditor affected by such legislation. Perhaps the statement made by the Central Banking Enquiry Committee, 1931, that "..... a real and lasting solution can only be found by the spread of education, the extension of co-operative and Joint Stock Banking and by the training of the borrower in habits of thrift and saving" is as true to-day as it was thirty years ago when it was made.

7. Direct Loans and Advances by the State.

The proportion of borrowings taken from Government is small, being only 3.3% of the total borrowings from all sources. Supply of agricultural finance directly by the Government was initiated as early as 1883 when the Land

Improvements Loans Act was brought into effect, and, was further stimulated in 1884 by the Agriculturists Loans Act. These measures were partly undoubtedly welfare measures; but, partly, they were also measures that led to the raising of land revenue and additional taxation on improvements in land secured through such loans. However, these advances, generally known as *taccavi* advances, were greatly circumscribed by rigid rules and regulations, and, though intended for enabling land improvements or relief of distress, became in the hands of unimaginative petty officials more a routine disbursement than an effective weapon for agricultural assistance. In fact, it is not wrong to assert that 'the record of *taccavi* is a record of inadequacies' for they were

(i) given in inadequate amounts,

(ii) based on inadequate principles of equitable distribution,

(iii) disbursed on inadequate recognition of appropriateness of security,

(iv) delayed and made uneconomic because of inadequate recognition of the conveniences of the borrower.

Apart from these defects, the more important shortcoming was that little attempt was made to follow up the loan with proper supervision as to its utilisation for productive purposes. Further, by the very nature of the governmental system of lending, strict adherence to material collateral security was insisted upon so that, by and large, it was the bigger cultivator rather than the needy small cultivator who benefited from these disbursements. The Reserve Bank's Rural Credit Survey General Report expressed dissatisfaction with the disjointed working of *taccavi* loans and suggested that it should be strictly limited to relief of distress. This suggestion, of course, is not a new one, for as early as 1901, the Indian Famine Commission had expressed the view that:

> "The policy of the Takavi Acts should not be regarded as productive merely, but also as protective; and it is upon the protective aspects especially that we would insist."

The concept of Government refraining from extending financial assistance on the theory that such loans destroy the spirit of self-help is an exploded theory, for to-day not only is the Government a people's elected and national government, but the welfare policy of the State has now been extended even to the idea of state partnership in co-operative rural credit at different levels.

8. Conclusion.

It has been pointed out that cheap and easily available credit is not the only, or even the best, solution for the ills from which the Indian Agriculturist suffers to-day. Undoubtedly credit and borrowing are necessary features of any commercial operation, and, if agriculture is to benefit from modern trends of business it is necessary to make it a paying industry by removing the impediments to efficient production* and convert it into a business rather than a mode of living. It is necessary to emphasise that :

> "Credit alone cannot convert an unprofitable industry into a profitable one. Credit may enable an individual to make a certain operation pay which might not otherwise pay or might not otherwise be undertaken at all and the price (of credit) which the producer has to pay may just turn the scale towards profit or loss in his own case. Viewed in this way credit may be an important factor in the cost of production in individual cases but it is mainly in other directions that a solution must be sought of the difficult problem of how agriculture generally can be made to pay..."

It is, however, true that proper credit facilities and proper economics of agriculture are interdependent, and, the development of the one assists, and is assisted by, the development of the other. The near-stagnant conditions of life in our agricultural economy are the root cause of our agricultural poverty ; credit, by itself cannot overcome this fundamental obstacle to our economic progress, and, it would be unwise to forget that : .

> "The problem is not merely one of making the existing economic institutions work more efficiently, or making small adjustments in them. What is needed is a transformation of the system so as to secure greater efficiency......"

*for causes of low agricultural productivity in India, see Vol. I Ch. 4 para 3. 2. 3

IV

THE CO-OPERATIVE MOVEMENT

1. **Co-operation—its basic concept.**

1·1 George W. Russel, writing more in a politico-philosophical strain than in a purely economic one, stated in his Co-operation and Nationality that "......the civilization which is based on individualism is mean, and the civilization based upon great guilds, fraternities, communes and associations is of a higher order. If we are to have any rural civilization, it must spring out of co-operation." It is no part of a study in economic assessment to value the civilizing influence of co-operation *vis a vis* its economic benefits, though undoubtedly from the social point of view one must prefer a given aggregate of welfare through co-operatives as compared to an equivalent one achieved otherwise, if one agrees with George Russel that "Sometimes one feels as if there were some higher mind in humanity which could not act through individuals, but only through brotherhoods and groups of men." It was this evaluation of aggregate welfare that Marshall[35] had in mind when he unequivocally held that "Even constructive competition is less beneficial than ideal altruistic co-operation." In the limited field of the co-operative movement, however, one looks to its economic advantages, for it has to be recognised that normally a group of individuals would prefer voluntarily a particular mode of conducting their business only if it is to their conomic interest to do so, as it is perhaps as difficult to persuade worldly men and women to cooperate and suffer a loss as it is to make water flow uphill.

1.2. The concept of the movement has been succinctly brought out by C. R. Fay in his definition :

> "Co-operative Society is an association for the purpose of joint trading originating among the

35. Principles of Economics, p. 9.

> weak and conducted always in an unselfish spirit, on such terms that all who are prepared to assume the charge of membership may share in its rewards in proportion to the degree to which they make use of the association."

The definition brings out that a co-operative organization is :

(a) not a charity organization, because it is concerned with free men in self-regulated action emphasising the idea of self help ; hence, the act of association is both voluntary and a recognition of equality ;

(b) in essence an orgnisation for an economic benefit to be secured through trading in the widest sense of the term ;

(c) not a seeker after particularist or sectional privilege for it must conduct its business for the benefit of all who join it in an unselfish spirit ; and,

(d) more concerned with the user rather than with his wealth for the benefites are commensurate with the use made *i.e.* faith in the society displayed, rather than with the wealth *i.e.* capital invested.

In India, there has sometimes been a hazy confusion between co-operation as a means to increased welfare and co-operation as an end in itself because of its socio-political values. Thus the third Five Year Plan[36] asserts :

> "In a planned economy pledged to the values of socialism and democracy, cooperation should become progressively the principal basis of organisation in many branches of economic life......"

It is not clear why it should be so for surely 'the values of socialism and democracy' are not dependent on the economic life being organised on a co-operative system nor are they obviously beyond achievement without a co-operative structure. It seems, therefore, unwise to assert that "The socialist pattern of society implies the creation of large numbers of decentralised units......" for it does not do so ; it would be wiser to recognise that the cooperative structure is needed, not because it elevates mankind to a nobler being, though that elevation is certainly desirable in itself, but because, in addition, it makes for a more economic way of life that contributes to the primary aim of economic development, *viz.*, the raising of the level of living of the people.

36. p. 200

1.3 The distinction drawn above may lead the unwary reader into fallaciously concluding that the business aspect of Co-operation is the be-all and end-all of the movement and that if it leads to the economic amelioration of its members, one need not look for anything else. The social economist realises the need for combating poverty, for "the destruction of the poor is their poverty", which is neither necessary nor inevitable; and, the co-operative movement is intended, now as always, to combat this poverty which apart from its material ills has in no small measure contributed to the stagnation of the poorer classes. In short, "The peculiar feature of co-operation as a remedy for stagnation is that it is intended to meet not only the more obvious material evils but also the underlying moral deterioration to which the poorer classes have so long been exposed".[37]

1.4 The basic advantage of a co-operative form of activity may be summed up as follows:

(i) It eliminates destructive competition *inter se* as between the members themselves. A co-operative sales society, for example, would act as a single seller on behalf of all its members instead of each individual member competing with every other individual member in their capacity as individual sellers;

(ii) It enables the realisation of the advantages of large scale operation. A cooperative farm may enable the small cultivators to derive the advantages of mechanised cultivation which each individually could not secure; or, again, a co-operative store could purchase things wholesale to obtain the advantages of large scale buying;

(iii) It helps to pool the resources of individuals with small and limited assets and obtain the benefits of strength through unity, as for instance, a credit society functions by increasing the creditworthyness of individuals who otherwise have little asset;

(iv) It helps to create a feeling of self-help and solidarity, and enables its members to resist exploitation, not by social or political upheaval, but by circumventing some of the channels which lead to such exploitation; and,

(v) "......It combines high aspirations with calm and strenuous action,...... it sets itself to develop the spontaneous energies of the individual while

37. Maclagan Committee Report on Co-operation in India, para 1.

training him to collective action by the aid of collective resources, and for the attainment of collective ends.''[38]

2. The Co-operative Movement in India—its early phase.

2.1 The introduction of the movement in India was at the initiative of the Government and was, at first, confined to credit only. The Co-operative Credit Societies Act of 1904 had as its cardinal object the growth of a genuine Indian movement and, hence, deliberately restricted the movement not only to credit but also to the concept of unlimited liability for rural societies. The chief features of this Act may be summed up as follows :

(i) The societies were given a legal personality and authorised to raise funds and carry on their business in a corporate capacity ;

(ii) The societies were to be audited annually and an official audit was made compulsory ;

(iii) The societies could advance loans to members only on personal or real security, but not ordinarily on security of movable possessions ;

(iv) The societies could give to its members only a limited interest in its share capital ;

(v) The societies were exempted from the provisions of the stamp Act, the Registration Act and the Income Tax Act.

2.2 The early success of the movement led to the Co-operative Societies Act of 1912 which extended the movement to other purposes besides credit and removed the earlier distinction between rural and urban societies. It also legalised registration of societies other than primary ones in the form of unions, Central Banks etc.

2.3 Subsequent development of the movement till 1947 was on stereotyped lines and more emphasis appears to have been put on quantitative expansion rather than on qualitative improvement. The movement became more and more officialised with the growing importance of the Registrar and his department.[39] A variety of societies were brought into existence but even in 1950 it was essentially a rural credit movement for credit societies constituted as much as 65% of

38. Marshall—Memorials p 227.

39. See para 2 of Annexure B of Cooperative Policy and Formulation of Supplementary Plans for 1959-63 (Ministry of Community Development and Co-operation)

the total number of primary societies. The second World War gave a fillip to the growth of consumer's stores and industrial Co-operatives and with the initiation of Community Development and Planning, Co-operation may be said to have received a fresh start and a new orientation.

3. Co-operation and Planning.

3.1 With the advent of planning and the growing participation of the state in welfare activities, the role of the co-operatives steadily expanded. It was but natural that the co-operative societies should become the chief agencies for state action, especially with the growing emphasis on non-official local leadership. The Community Development Programme is an all embracing scheme and aims at the improvement of all aspects of life—economic and social. Its primary function is to arouse the people themselves and hence the Panchayats and the Co-operatives must logically be the chief agencies for carrying out the programme. In the field of planning, it has been recognised that "Economic development and social change are equally vital elements in the reconstruction of India's social and economic structure." The Third Five Year Plan[40], therefore, categorically states :—

> "Co-operation is one of the principal means for bringing about changes of a fundamental nature within the economy. As was stated in the Second Five Year Plan, in a country whose economic structure has its roots in the village, cooperation is something more than a series of activities organised on co-operative lines ; basically, its purpose is to evolve a scheme of co-operative community organisation which touches upon all aspects of life. Within the rural economy, in particular, cooperation is the primary means for raising the level of productivity, extending improvements in technology and expanding employment so as to secure the basic necessities for every member of the community."

3·2 A sovereign democratic State has a responsibility for promoting the welfare of its people, and the co-operative movement has an important role to play in assisting the realisation of the true ends of a Welfare State.[41] A Co-opera-

40. p. 200.
41. See Bose, S. K.—Planning in Modern India—need for reorganisation of the co-operative Movement, Orissa Co-operative Journal, September 1953.

tive Society can be, and should be, the medium for educating public opinion for an effective demand for a higher standard of living, and, obviously is also the best means of executing many of the activities of economic and social uplift that are planned for national development. But no plan of a Government can succeed in a vast country like India unless it is adopted by the masses and becomes a part of the ideology and the very thinking process of the people. Only a co-operative society could reasonably hope to be an agency for ensuring such results. It is, however, obvious that with national planning, general policy directions and guidance must come from the State which must also regulate the basic structure of the movement and provide the broad framework of the law within which it must work. But to be really successful, the movement must be both broadbased and popular and it could not be either unless it was voluntarily brought into existence by people who regard it as their own creation. In short, the co-operative movement must be a people's movement with local leadership occupying responsible positions in it, with local initiative organising it and members themselves running it.

3·3 The criticism that "in some States, the Government and its officers have often not encouraged local leadership to come into the movement in responsible positions in the belief that they were not really capable of organising and running it" is, in a sense, an admission of the failure of the policy of State sponsoring of co-operative activities, and, the sooner there is a change of outlook the better it is. It is, therefore, heartening to note the view[42] that :

> "Every effort must......be made to encourage the people and their leaders to take over the organisation and running of the movement. Government will, no doubt, continue to perform its statutory functions under the law and give the maximum possible financial and other assistance. The objective, however, should be to transfer, as early as possible, the responsibility for the movement to the people and their leaders."

In fact, it is surprising that even ten years of planning has not yet succeeded in giving a firm popular bias to the co-operative movement, probably because in an anxiety to speed up quantitative expansion of the movement, Registrars were more concerned with societies than with men, more with successful working than with workers, more with avoiding liquidation than with liquidating societies that did not

42. Vide 39.

produce men to run them. It is necessary for those who are handling co-operative policy to recognise that if co-operation is to succeed we must develop co-operators and not merely co-operatives for "Once the processes of social and economic change gather force and the rural community attains higher levels of skill and productivity, co-operation has to meet larger and more complex demands;" and, this cannot de done unless we have co-operators.

4. Structure and Organisation of the Co-operative Movement.

4·1 Co-operation is a way of life; it is a method for organising group activity and, therefore, as long as the activity is legal one could organise a co-operative society to further the interest of the members in that field of life. Generally, however, a Co-operative way of pursuing an activity is prompted by a desire to gather strength by unity, and, hence, it is a way of organising economic activity for those who are economically weak. The very concept of a Co-operative Society involves the implicit assumption of a fair degree of mutual knowledge amongst its members so that it tends to be restricted in size and confined to a more or less harmonious group of people tied together by common needs and common characteristics. There are certain forms of co-operative activity where these limitations may not operate, as, for instance, in a Consumer Store or in a multi-purpose society, where the size could be much larger and membership lacking in compactness as compared to societies where, as in a credit society or a marketing society, mutual knowledge and trust are essential. The controversy about the ideal size of a primary co-operative society is really a profitless war of words, for the size of a co-operative society is to be determined by its nature and the functions it has to perform, and not by any theoretical considerations of optimum number of members or area to be served. It could have any size provided the essential characteristics of a co-operative society are ensured *viz.*, voluntary basis, mutual knowledge and mutual trust, homogeneity of outlook and group benefit with a social purpose.

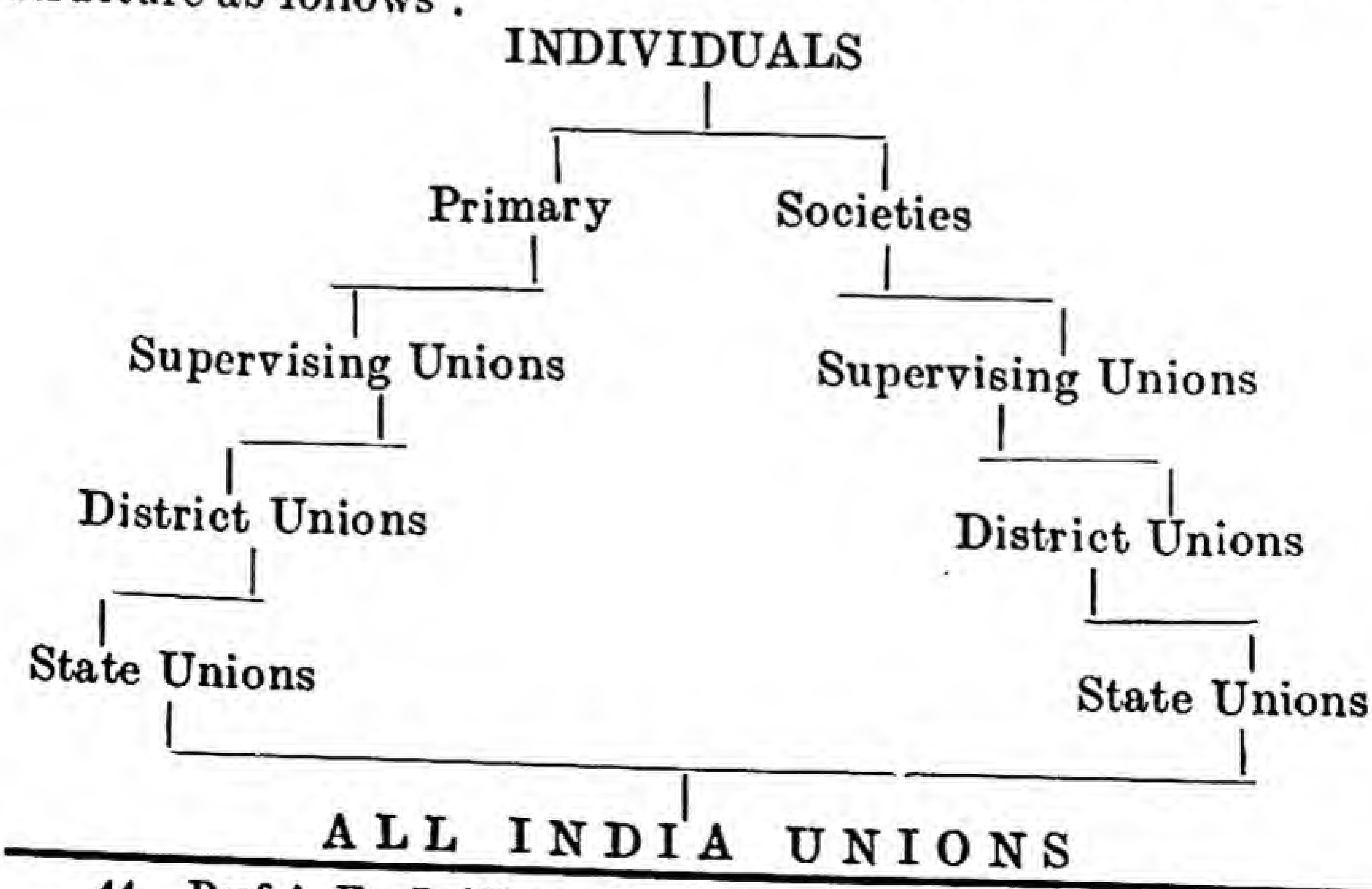
4·2 An important question that often is the subject-matter of considerable controversy is the question of what is loosely called "open" membership. It is sometimes maintained[43] that :

> "It is......essential that every person, who wishes to join a co-operative organisation and benefit by it, is enabled to join it. To ensure this, it is necessary to give him a right of appeal against the refusal by the society to admit him as a member."

44, Vide. 39, para. 9 (i).

This view, apart from being vague and hazy, is both unscientific and against the inherent concept of voluntariness implicit in a co-operative organization. The view quoted above is hazy as it does not say to whom the appeal will lie and whether the appellate authority can "force" the society to accept an individual whom it is otherwise unwilling to admit. Presumably this power will lie with the Registrar or with Government for a co-operative society is an autonomous sovereign body. If, however, the Registrar or the Government are to thrust an individual into an unwilling society (whatever the reason for that unwillingness and however justified or unjustified it may be) surely the very basis of compactness and mutual trust would be shattered and the seeds of failure laid. Further, neither the Registrar nor the Government (nor any other authority which may perform as appellate authority) could accept the liability of failure consquent on their decision and, if so, it would lead to a paradoxical situation in which a society has to accept a decision contrary to its wishes and also face its consequences. If official agencies are to accept the responsibility for determining eligibility for membership then obviously "......the trend is towards greater government control in the immediate future, and that the dream of ardent co-operators of the last generation, that the movement would some day become truly popular, is now more remote than it was before independence."[44]

4·3 Planning in India is a national integrated process, even though individual schemes are operated by States and the Union Government. Similarly, even though co-operative societies are individual autonomous bodies, interlinking of their activities would be desirable for the sake of planned coordination. One may, therefore visualise an integrated structure as follows :



44. Prof A. F. Laidlaw—Report to the Central Committee for Co-operative Training, p. 25.

The above structure visualises the idea of an effective integrated policy with adequate recognition of local requirements at all levels. The success of any such integration would require :

(a) sound societies at the base ;

(b) membership at all levels of co-operators in the true sense of the term ;

(c) eschewing of political influence, if any, in all its aspects ;

(d) freedom from Governmental control in day to day operation ;

(e) emergence of true popular leaders in charge of the movement at each level.

4.4 *Types of Societies.* Classification of the various types of co-operative societies is apt to be always artificial as it would depend on the point of view and, in many cases, overlapping of functions are likely to take place. In any case, there is an endless variety of societies for there is an endless variety of wants which could be furthered through the Co-operatives. Broadly, however, the following grouping may give a fair idea of the movement in India.

A. Agricultural.

I Credit.

(i) primary credit societies.

(ii) Land Mortage Banks.

(iii) grain *gollas*.

II Non Credit.

(i) special purpose Societies—*e.g.* Land Reclamation, Consolidation of Holdings, Co-operative Farming etc.,

(ii) general purpose societies—e.g. co-operative stores, Purchase and Sale Societies, Marketing Societies etc.

(iii) non-economic functions societies,—*e g.* educational societies, sanitation societies, anti-malaria societies etc.

(iv) multipurpose societies.

B. Urban.

III Banking and Credit.

—Urban Banks, Industrial finance societies, thrift societies etc.

IV Non-Credit—(a) general.

Consumer's Stores, Production societies of artisans and craftsmen etc.

(b) Specific purpose.

Housing Societies, Educational facility provisions, unemployment aid etc.

C. Financing.

(i) Central Banks,

(ii) Provincial or State Banks,

(iii) Guaranteeing Unions,

D. Special Activities.

(i) Insurance,

(ii) City Milk Supply,

(iii) Operation of Capitalistic Industries,

(iv) Cottage and Small Scale Industries Co-operatives.

It is clear from the classification given above that there are no specified functions for which cooperative societies can or cannot be organised ; for every imaginable type of activity one could envisage a co-operative society, for cooperation is only a manner of supplying the needs of a group of people.[45]

5. Some Problems of the Co-operative Movement.

5.1 *Simplification of Cooperative Law and Procedure.* The Constitution of India, *vide* item 32 of the State List of the Seventh Schedule, makes cooperative societies a State subject. It has been so since 1919 when the Constitutional reforms included it in the transferred subjects. Some States have passed laws of their own while some are still working under the 1912 (Central) Act with local legislative amendments. The various State laws naturally lack a certain degree of uniformity, sometimes even in fundamental respects, since economic and social conditions vary from State to State. With the growing reliance on cooperative organizations in the realm of planned development, which itself is a national integrated process, it is desirable to have a certain degree of uniformity in cooperative legislation, even though in matters of detail it might differ from State to State and incorporate local features to take account of regional requirements. The law relating to the cooperative movement

45. See Bose, S.K.. Cooperation in Progress—our sytsem analysed, Orissa Cooperative Journal, March, 1953.

should normally lay down broad principles so as to ensure the cooperative character of the institutions and indicate the functions of the Statutory authority. It is now generally recognised that functions of the Registrar—the Statutory authority—should be restricted and should be confined to—

(i) audit,

(ii) liquidation and supersession,

(iii) voluntary winding up, and,

(iv) inspection, especially utilisation of financial assistance received from Government.

After nearly half a century of unfettered control over the cooperative movement, the suggestion that the powers of Registrar of Cooperative Societies should be curtailed* may seem shocking, but is essential if the movement is to ever become what is was intended to be, *viz.*, a people's movement governed by the people. Recent trends in the movement have led many to believe that the existing large measure of government control over cooperatives in India is on the increase,—a trend which all true cooperators deplore. The following quotation from Prof. Alexander Laidlaw's Report to the Reserve Bank of India's Central Committee for Cooperative training (para 71) would illustrate the point :—

> "......Cooperative departments, their officers and the governments which they represent are becoming more firmly entrenched as the real power in control over cooperative societies. A vested interest of officials has been created which is going to take considerable time and great effort to dislodge. I found the attitude in some quarters that government should not relax its control over the movement and that official direction from the top will have to be continued indefinitely in the cooperatives in India."

Prof. Laidlaw's report was submitted in October 1958—eleven years after independent India come into being, and no severer condemnation could have been made of our misguided guardianship of the co-operative movement. If the movement is to survive, it must be freed from the tentacles of official control which, in the name of efficiency, have been squeezing out the life blood of true cooperation. The broad lines on which cooperative legislation should be modernised and liberalised are :

* This could, of course, also be done by voluntary restraint; as Registrar in Orissa, I never interfered in the day to day working of a society for I believe that it is only by making mistakes that true Cooperators are born.

(a) provision for association of non-official element in policy formulation at the State level ;

(b) facilities for amalgamation and division of societies with the consent of the members concerned ;

(c) prompter execution of awards, decrees and orders concerning cooperative societies ;

(d) quicker facilities for registration at local levels ; and,

(e) representation of financing Central Banks on the managing Committees of the more important societies.

5.2 *Training of Cooperative workers.* To educate men and women to a cooperative way of life is something more than to impart training on the rules and byelaws of a society or on how to run it efficienlly ; it involves developing in the people a faith in cooperation not merely as a means to end but even as an end itself. Enlarging the cooperative sector is a part of planned development in India and to achieve it we must have an army of ardent cooperators who would effectively help to run the cooperatives. In a sense, one could distinguish between two aspects of the problem *viz.*, (a) those relating to the non-offical cooperator, and (b) those relating to the official staff engaged in cooperative work. The importance attached to the problem of training has been of sufficient importance to justify the setting up of a Central Committee for Cooperative Training by the Government of India through its Resolution of 2nd May 1959. However, it must be admitted that it has perhaps not yet been fully appreciated that the new social order that India is planning to build up can be established only by the people being cooperative-minded rather than by a host of government employees being trained or reoriented. Finally, the training programme must recognise that "while it is true that cooperation rests on high idealism and dedication to noble principles, it also depends on hard-headed business practices that must be learned by those who want to make the ideals of the movement come true."

5.3 Credit and Finance.

5.3.1 The origin of the cooperative movement in India was prompted by the need to supply credit to the agriculturists. The early sponsors of the movement had hoped that cooperative credit would in course of time, replace the moneylender and free the cultivator from the tentacles of an unproductive indebtedness. We have seen (*vide* Ch. III, para 6.4.1) that even after more than half a century, the

cooperative movement has not been able to supply even 4% of the total requirements of the borrowing needs of the cultivator. The increase in the total volume of advance from the cooperative societies, apart from its inadequacy in relation to total needs, is hardly an index of its meeting the requirements of the needy cultivator for one of the revealations of the Reserve Bank's Rural Credit Survey was that the major portion of the funds of the co-operative societies went to the bigger cultivators. There was nothing startling or unexpected in this fact, since it was an obvious corollary of the policy of assessing creditworthyness in terms of material assets—a development that was completely different from what was envisaged for the Government of India Resolution of 1914 clearly stated that "The Indian Act of 1904 was admittedly intended to encourage small and simple credit societies for small and simple folk with simple needs......the chief object held in view from the beginning has been to provide reasonable credit for small agriculturists, who represent the backbone of the Indian polity". If subsequent developments have led to a deviation from the original accepted ideal then it can only be attributed to a failure on the part of the official machinery that was incharge of the movement. In fact, so outstanding has been this failure that the National Development Council's resolution of 1958 on co-operative policy directed that "co-operative credit should be made available on a liberal scale and on terms suitable to all farmers, especially to those not able to obtain credit under ordinary commercial banking principles." It is, however, obvious that there is nothing new in the idea that creditworthyness is, for co-operatives, not a reflex of material possessions but honesty and productivity for as has been aptly said "co-operative credit is capitalising honesty."

5.3.2 Extension of the role of credit is implicit in the very conception of the increasing use of co-operatives in our planning. The widening of the ambit of co-operative credit involves enabling co-operative societies to admit all classes of cultivators and to make available adequate finance at reasonable cost. Such an extension would imply including marginal and sub-marginal cultivators, landless tenants and other 'assetless' persons as members and to make available to them adequate credit on the basis of their production requirement and repaying capacity rather than on the valuation of their material assets. An important question that has been raised recently is that relating to financial support for cooperative societies by State participation in share capital Before, however, discussing this important and revolutionary extension of State aid to co-operatives in India, it would be

desirable to understand the sources of finance for co-operative credit societies.

5.3.3 The soures of working capital of primary credit societies may be classified as follows :

(i) Share capital,

(ii) Deposits from members and non-members,

(iii) loans from societies, Central Banks and from Government or Reseve Bank,

and (iv) Reseve fund.

It is clear that the first two sources must, by the very nature of the conditions in India, be of a limited character and could not be expected to contribute much as the saving of the rural people itself is limited. The same could be said of No (iv) *i.e.* Reserve fund which could only grow with a large volume of business; however, since both the volume of business and the profitability of whatever limited loan operation that a credit society undertakes is generally small, the contribution that Reserve fund could make to the working capital of the society is strictly limited. In a sense, one would, therefore, be compelled to conclude that most societies in India must work with borrowed funds, the volume of which would be determined to a great extent on the borrowing capacity of the society, and, the important question that would then arise is the problem of what determines this borrowing capacity. In any case, there is no denying the fact that credit societies in India never had sufficient working capital to meet all the demands that were made on them and it is the shortage of the credit facility available that led to the growth of the policy of State participation in the share capital of co-operative societies.

6. Public Aid and the Co-operative Movement

6·1 The Maclagan Committee on co-operation concluded that "the attitude of the Government is that it disclaims all financial responsibility and makes no definite promise of monetary support. This policy is based on a desire to establish a genuine co-operative movement which shall be self-contained and self-supporting, and, in so far as it represents the rejection of a system of money doles or undue special concessions, it appears to ..be a correct and desirable policy". To the ardent co-operator the concept of dependence on State finance with its logical consequence of interference and political pressure, is against the very principles on which co-operation is based and is to be avoided. The evils of State help are ;

(i) It curtails the freedom of the movement and takes away the basic concept of self-help ;

(ii) it fosters leisurely and irresponsible work and often is the source of bad debts ;

(iii) it makes facile availability of resources and tempts uneconomic utilisation by inculcating the fallacy that co-operative banking is not governed by the same basic laws of finance as ordinary banking ;

(iv) it fails to develop true leadership ; and,

(v) it causes infiltration of party politics into a co-operative society.

It is, of course, not denied that the State may create conditions for sucessful development of co-operatives by special legislation, by arranging for independent and strict audit, by providing assistance in the form of guidance or even keeping accounts accurately, but when State aid enters the realm of direct financial assistance it enters a dangerous phase which true lovers of co-operation must strive to avoid.[46]

6·2 Recent trends in India are, however, towards more direct participation by the State in the co-operative movement, even to the extent of contribution to the share capital of societies. The present trend of co-operative policy supports contribution by Government to the share capital of credit unions, Apex and Central Banks, marketing and processing societies, though it refrains from State participation in the share capital of village societies. Even for the latter, the Third Five Year plan expressed rather strange views, *viz* :

(a) the state could participate if

(i) 60 percent of members desired it,

(ii) the affiliating Central Bank supported it,

(b) a maximum of Rs. 5000, and in exceptional circumstances Rs. 10,000 was laid for such participation,

(c) the participation should normally be indirect, that is, through apex and central cooperative banks.

These views are strange and almost self-contradictory for while it recognises the possibility of opposition from some members, it also wishes to "thrust" such assistance through the cooperative medium *viz* the financing banks. It recognises that such schemes of assistance are slippery and, therefore, may lead to a system of nominated

46. See Bose, S.K.—Aided Co-operatives, in All-India Co-operative Review, February, 1955.

directors, and hence attempts the impossible compromise by suggesting that :

> "where, for special reasons, State participation in share capital is direct, nomination of directors to the managing committees of primary societies should be avoided. If such nomination is considered essential, the authority to nominate directors should be delegated to central cooperative banks."

Such direct participation in the share capital of cooperative societies are, definitely and completely, unmixed evils. It is necessary to recognise that the State in a modern democracy is synonymous with the political party in power, and it is unwise to bring the cooperative movement within the fold of a fluctuating policy determined by ideologies far removed from basic cooperative principles.

6.3 State participation in cooperatives has in recent times been advocated on the need "to admit all classes of cultivators" into the fold so that the following basic advantages may follow :

(i) a supplementary line of credit can be made available with a view to implementing village agricultural production plans,

(ii) prevent the cooperatives from becoming preserves of the material asset-holder,

(iii) encourage the small cultivator, particularly those in possession of uneconomic holdings, from joining cooperative societies and effectively benefitting from them, and,

(iv) combat effectively vested trading interests through a properly coordinated credit and marketing scheme, especially through the crop-loan schems.

These features were broadly incorporated in the integrated scheme of rural credit propounded by the All-India Rural Credit Survey Committee of the Reserve Bank of India. The need for extension of credit, especially to those not in a position to provide appropriate collateral security, has been recognised in the Third Five Year plan which has made an important recommendation in this respect, *viz.*,

> "To enable cooperative societies to admit all classes of cultivators, including marginal and sub-marginal cultivators, landless tenants, etc. as members, and provide them with adequate credit on the basis of their production requirement and repaying capaci-

47. Ch. XIII, para. 8.

ty......the State Governments should make an outright contribuion to the funds of each society at 3 percent of the additional loans made during the year over those advanced by it in the preceding year. An outright contribution of 1 percent to bad debt reserves should be made to central cooperative banks in respect of the additional finance provided by them. In the intensive agricultural districts, where credit is sought to be made available to the full scale of requirements, the outright grants are at a slightly higher level, being 4 percent for primary societies and 2 percent for central banks. The continuance of these outright grants is contingent on the condition that the weaker sections of the community, who have hitherto been unable to get adequate credit, should now receive the necessary assistance. The outright grants received by primary societies and central banks were to be credited by them to special bad debt reserves which would be in addition to the normal bad debt reserves created from profits. It is envisaged that at an appropriate stage, a careful assessment of the extent to which outright grants have led to the extension of credit facilities, should be undertaken" [47]

The above scheme is in a sense only a limited extension of the idea of assisted credit to stimulate productivity based on creditworthyness derived from potential repaying capacity. To the extent the extended loans are based on true and correct assessment of repaying capacity, they would be productive and would need no subsidisation by the State ; to the extent they contribute to bad debts because *prima facie* they were unproductive investments, State subsidisation would only weaken the cooperative movement—probably financially, certainly morally.

6·4 Provision of credit for agricultural production plans at the village level is obviously a complex problem, specially as there is little experience available in this respect. Ultimately it is a problem of increasing the borrowing capacity of the members, and, the most effective way of achieving it is to link up credit with intensive production plans of a large number of families together with the marketing of the produce. Such a scheme may be expected to

(i) ensure prompt repayment,

(ii) expand share capital,

47 Third Five Year Plan, p. 203

(iii) enlarge reserves, and

(iv) attract more local deposits.

Increase in the internal resources of a society must take time and, hence, a supplementary line of credit has to be made available which would mainly be intended for seed, fertilisers and current expenses of cultivation but may also include medium term loans of approved types. The question of responsibility for such extended credit in the event of non-recoverability is an important one. It is held in certain quarters that since funds are made available by the Reserve Bank at lower rates of interest than those at which other funds are borrowed, there should be available a margin from which losses, if any, from extended credit should be met so that apex and central banks should be able to accept the responsibility for these losses. It may be pointed out that such reasoning is based on a fallacy and confuses ability to meet a loss with the prudence of accepting such a liability in principle; for obviously, such extended credit must be, by its very nature, beyond the limits of prudence which the co-operative society would have, of its own accord, accepted.

7. Special Funds for Medium and Long-term assistance.

7·1 One of the important recommendations of the Integrated Rural Credit Scheme was the creation of special funds under the Reserve Bank and the Government. These were :

(a) the National Agricultural Credit (Long Term Operations) Fund to enable the Reserve Bank to give financial accommodation to State Governments and to land mortgage banks ; the funds made available to State Governments were to be used for participation in the share capital of co-operative banks, credit societies and land mortgage banks ;

(b) the National Agricultural Credit (Stabilisation) Fund for granting medium-term loans to State Co-operative Banks ; assistance from this fund would be specially available if overdues in short term loans granted by the Reserve Bank came about consequent on famine, draught or other calamities;

(c) the National Agricultural (Relief and Guarantee) Fund to be operated by Government for providing assistance for writing off irrecoverable arrears of co-operative societies arising from chronic natural distress ; the assistance is to be made available to

co-operative institutions as grants through State Governments.

7.2.1 Of the above three funds, the first two are in the nature of medium-term advances by the Reserve Bank while the last one is a sort of a special State aid to co-operatives to meet losses arising out of conditions beyond their control. The general problem of financial aid from Governments to cooperatives has already been considered earlier. It is difficult to accept that members of a co-operative society are entitled to receive special consideration from the taxpayers while non-members affected by similar calamities are not so entitled, and, in principle, such assistance is objectionable as they tend to enhance the dependance of co-operatives to State assistance and may reduce their independence and autonomy.

7.2.2 In 1955 the Reserve Bank of India Act was amended to enable the Bank to provide large financial resources to assist reorganization and development of co-operative credit. In accordance with the amendment, the National Agricultural Credit (Long-term Operations) Fund was established to be drawn upon for advancing :

(a) medium-term loans to state co-operative banks,

(b) long-term loans to state governments for contributing to the share capital of co-operative credit institutions,

(c) loans to central land mortgage banks and purchase of their debentures.

Prior to the establishment of the Long-term Operations Fund, the Reserve Bank could issue medium-term loans to an aggregate of Rs. 5 crores and restricted the quantum available to any State co-operative bank to an amount equal to the banks owned funds ; the latter, in turn, being advised to limit advances to the extent of the owned funds of the central co-operative banks. The restrictions imposed on the Reserve Bank were removed in 1955, though the advice given to State co-operative banks to restrict medium-term advances to their affiliated banks to the extent of the latter's owned funds was continued with a view to :

(i) avoiding resort to medium-term loans for short term purposes,

(ii) preventing seasonal agricultural operations through medium-term loans,

(iii) ensuring utilisation of long-term funds available with land mortgage banks,

(iv) developing fully the resources raised by the co-operatives themselves as obviously the loans provided by the Reserve Bank are intended only to supplement those already provided by the co-operative sector itself.

It has, however, to be admitted that the Reserve Bank itself has not been able to utilise fully the resources available under the Loan Operations Fund, the position of which on June 30, 1959 was as follows :

(In Rs. crores)

Balance to the Credit of the Fund		30
Less Amount outstanding	19·40	
+		
Limits operative	1·64	
Balance available for	21·04	
distribution	8·96	

8. Land Mortgage Banks and long-term Credit.

8.1 The normal credit needs of the cultivator includes longterm credit for obtaining fixed capital to be invested permanently or for long periods in :

(i) purchase of land,

(ii) acquisition of costly equipments,

(iii) consolidation and improvement of holdings, and,

(iv) making permanent improvements in the productivity of land.

In addition, the cultivator in India requires long-term funds to redeem his prior debt which, in a sense, is unproductive borrowing, though maybe unavoidable if he wishes to retain his land and continue to make at least such a living as he has been doing in the past. From the strict economic point of view there is little difference between borrowing to purchase land and borrowing to redeem the ancestral debt to prevent sale of land for the productivity and economies of either would depend on the terms of the "investment" and on the availability of alternative means of earning a livelihood. To be economic, long-term rural credit must satisfy two conditions, *viz* :

(a) Sufficiency, *i.e.* adequate to effectively start the operation intended, and

(b) Self-repaying i.e. repayable from the margin of profit of the borrower's holding without the necessity of

(i) starving his current financial needs,

(ii) alternative and additional borrowing,

(iii) having to sell his assets to discharge the loan.

The concept of long-term credit is to be linked more to the purpose of the loan and the repaying capacity of the borrower rather than to any defined period of time. In many countries the essence of a long-term loan is to make its recovery in instalments that are only a small percentage of the principal amount of the loan by spreading its recovery over a long-term of years which range from 30 to 75 years. It is, however, clear that while a maximum period for recovery should be laid down, the minimum period should determined by the additional yield following from the stment and need not be uniform for all borrowers.

8·2 It has generally been recognised that normal banking institutions, whether commercial or cooperative, are unsuitable agencies for longterm credit. It has, therefore, been necessary to develop special types of credit institutions for long term financial needs of the cultivators in the form of land mortgage banks. It is not necessary that such institutions must be necessarily cooperative, though in India the trend has been continuously towards the formation of co-operative land mortgage banks which are more suitable for providing relief to small agriculturists and owners of small holdings. In India, however, the type that has mostly come up maybe regarded as a quasi-co-operative type tending towards the pure co-operative type since quite a few of the land mortgage banks are associations of both borrowers and non-borrowers with unequal share capital held by the different members though each member has a single vote irrespective of his share capital. In a sense, the scope of a purely cooperative organization in the sphere of land mortgage banks is rather limited for mortgage credit is extremely impersonal and is devoid of the human element as far as possible. A successful land mortgage bank must depend more on sound valuation of security, careful investigation of titles, correct assessment of borrowers credit and repaying capacity and efficient financial management than on idealistic concepts of removal of borrowing disabilities, potential repaying capacities and moral reform of the borrower.

8·3 With the development of cooperative land mortgage banks an important question that arises is the extent and nature of state aid to be granted to such institutions. It

may be pointed out that the case against State aid is stronger for normal co-operative societies than for mortgage banks even when registered as co-operative societies for the simple reason that the pure co-operative element is less in a mortgage bank. Further, the chief objections to State aid are when it is directly financial, but other forms of aid are both suitable and necessary for mortgage credit banks. Government assistance to land mortgage banks may take the following forms :—

(i) guaranteeing the interest on debentures issued,

(ii) including the debentures of these banks among trustee securities,

(iii) purchase of such debentures by Government,

(iv) guarantee of the titles to the land by the State,

(v) granting of the power of foreclosure with a speedy foreclosure procedure, and, of sale without recourse to law courts.

8·4 The growing importance of the Central Land Mortgage Banks in the country has been a source of considerable satisfaction since these institutions are the main source of long-term credit to the agriculturist. The following figures indicate their growth :

(In Rs. Lakhs)

Year	Working Capital	Fresh Advances
(1)	(2)	(3)
1951-52	1,016·58	250·65
1954-55	1,578·82	243·49
1956-57	2,132·47	380·22

It will be seen that the rate of growth of working Capital has been faster than fresh advances showing perhaps that during the first plan period at least some limitation in expansion were noticeable. Of couse, in addition to central land mortgage banks we have in India primary land mortgage banks which also supply a fair amount of finance. However, the position as at the end of June 1960 was as follows :

(In Rs. thousands)

State	Working Capital	Total loans	Overdues
Andhra Pradesh	81836	58270	*
Assam	1542	1409	42
Bihar	1070	190	*
Gujarat	82959	72019	7502
Kerala	10992	9587	61
Madhya Pradesh	5629	3071	353
Madras	79281	52843	*
Maharashtra	56968	44216	2340
Mysore	38392	31362	138
Orissa	6926	5727	18
Punjab	3025	3708	*
Rajasthan	623	71	*
Uttar Pradesh	1501	N.A.	*
West Bengal	2956	2478	*

* Negligible.
Source—Reserve Bank of India.

9. Co-operative Marketing.

9.1 The All-India Rural Credit Survey Report of 1951-52 recommended integration of Co-operative Credit and Co-operative Marketing as an important measure of rural finance. An integrated approach to credit and marketing is a natural corollary to the fact that India itself is the main market for her agricultural produce. Apart from specific disabilities like manipulated scales, weights and measures, unjustified deductions and extractions, unfair bargaining and deliberate under-buying by "pooled" dealers from which the cultivator suffers due to lack of adequately regulated markets, he suffers most from his economic inability to obtain a fair price because of

(a) internal competition to sell ;

(b) anxiety to sell quickly due to.

  (i) absence of holding power,

  (ii) absence of proper and economical warehousing facilities,

  (iii) unwillingness and inability to stay on and watch the market ;

(c) lack of proper grading facilities for determining the quality of his produce ; and

(d) lack of proper communication and transport facilities which prevent him from tapping the more favourable prices in the distant markets.

The need for proper marketing facilities is most needed in India because of the fact that marketable surplus* is small for each individual cultivater, though collectively it is enormous. The establishment and development of co-operative marketing societies has been considered an important measure for improving marketing facilities. In fact the Congress Agrarian Reforms Committee[48] went so far as to suggest that "......there should be compulsory co-operative marketing of all village agricultural products and no individual farmer would be allowed to sell his surplus independently." Genuine cooperators would, of course, find this mixture of "Compulsion" in co-operation an unacceptable paradox ; but, development of co-operative marketing would undoubtedly provide a solution to some of the problems for those who voluntarily join such a society.

9·2 Two important features of agricultural marketing conditions in India deserve special mention. These are :—

(a) the village buyer of produce at wholesale is usually also the chief source of credit-supply to the cultivator. We have seen that the moneylender, particularly the agriculturist money-lender, predominates in the supply of credit.† The cultivator is often compelled by circumstances to sell his produce to his creditor. As the Reserve Bank's Rural Credit Survey pointed out "The marketing of agricultural produce is largely in the hands of a body of men who,...... represent private interests and who control both the sources of credit and the disposal of the produce. Often enough, therefore, the cultivator's position is that of having to bargain, if he can, with someone who commands the money, commands the credit, commands the market and comes with the transport." It is obvious that under such conditions the cultivator can hardly expect to get a fair price, let alone a good price,

(b) There is generally an excessive number of middlemen who intervene between the cultivator and the final buyer, many of whom hardly perform much economic function. It is difficult to estimate the gap between the price

* See Vol I, Ch IV, Para 3.2·1.

48. Report p. 64, 105.

† See earlier, Ch, III, para 6.4.1.

received by the primary producer i.e. the cultivator and the general wholesale price of the produce in the big *mandis* and markets, but even if the rather conservative estimate of 15 percent is taken as the starting point, one would be compelled to admit that a big slice of the cultivator's reward has been taken away, particularly when the parity index is none too favourable to him.*

9·3 The fundamental characteristic of co-operative marketing needs to be understood properly. It is not the aim of a co-operative marketing society to raise prices by a policy of restrictionism ; it is essentially concerned with readier adjustment of supply to demand by stabilising marketing conditions through appropriate and orderly regulation of supply. In short, cooperative marketing does not seek to alter the results of competitive conditions by creating monopoly or cornering of supplies, but seeks to work within the free market and maximise the benefits to its members by eschewing as far as possible the disadvantages of the competitive system. The economics of price fixation in a competitive market is usually disadvantageous to the producers when they have a seasonal product which is perishable and which is supplied by innumerable individual producers acting independently. Such a condition not merely leads to a possible depression of price at harvest time, but also necessarily introduces an element of fluctuation in it since the supply of agricultural produce is seasonal while its demand, especially that portion of it which relates to foodgrains, is continuously steady.† A co-operative marketing society aims at combating such seasonal depression of price and wide fluctuation from time to time by a more effective adjustment of supply to demand.

9·4 A truly co-operative marketing society should not merely provide for democratic control but also distribution of earnings on the basis of business brought by members and transacted through the society. The most economic and appropriate method is to undertake pooling of supplies so that the identity of individual sources is done away with and each member receives a price calculated on his contribution to the pool and the average selling price of the product. It is necessary, of course, to have standardised grading so that the cultivator raising produce of a high quality does not suffer. It is necessary to emphasise that continued loyalty of individual members cannot be ensured without honest and efficient grading, even if the other

* Vide Vol I, Ch. V, page 215.
† See Vol I, Ch. V para 1.2.

activities of the society are carried on in a businesslike fashion. The Reseve Bank's follow up Rural Credit Survey[49] found that

> "Arrangements for storage......were not always satisfactory. Delay in effecting sales which involved additional expenditure for the cultivator made the problem of storage still more difficult. Grading of produce......was sometimes done unsatisfactorily and it was stated that the bigger cultivators and sometimes petty *traders cum cultivators* managed to get better grades for their produce. It was also reported that sometimes, the would be purchasers attempted to influence the staff who were in charge of grading so that produce would be given a grade lower than what it deserved."

These are serious deficiencies, the continued existence of which must inevitably adversely affect the loyalty of members, particularly the producer of the superior grade of the commodity. Human nature being what it is, it is foolish to assume that a co-operative spirit can grow merely by the formation of a co-operative society, for only through successful economic endeavour can one inculcate a love for the co-operatives and loyalty can only be secured by efficient service provided.

9·5 The Integrated Rural Credit Scheme visualised co-operative marketing societies

(i) arranging for the sale of produce of members,

(ii) providing pledge finance against produce brought by members,

(iii) recovering on behalf of the primary credit societies the crop loan advanced to members.

The essence of the scheme was to strengthen both the credit co-operative and the marketing co-operatives simultaneously, and, to contribute to the economic upliftment of the cultivators by providing better faclities for the marketing of their produce and at the same time providing them with interim accomodation, pending sale, in the form of pledge finance which is normally expected to increase their bargaining power. However, the entire success of the approach would depend on the ability of the co-operative movement to free the cultivator from dependence on private credit for the latter often compels sale through private traders. Thus, a weak co-operative marketing structure

49. General Review Report pp. 488-89.

retards further development of credit co-operatives while a weak co-operative credit structure must delay the efficient functioning of marketing co-operatives.

10. Progress and Achievement.

10.1 Assessment of the achievements of the co-operative movement is difficult for it is the one field of economic organisation where quality rather than quantity is important. It is unfortunate that in many of our recent discussions on co-operative development more stress has been laid on physical targets and inadequate attention has been drawn to the need for recognising that it is not the co-operative society which is important but the cooperator, it is not the number of societies registered that is the index of progress but the quality of service performed by them, it is not to the amount of credit disbursed to which we should look but its utilisation and effect on the borrower's productivity. It is, of course, difficult to make such an appraisal except through detailed study of the working and performance of individual societies. To make an appropriate study one would need the sort of pains-taking survey that the Reserve Bank undertook in its follow-up survey of 1956-57 which is admittedly both expensive and time consuming and can hardly be undertaken frequently. However, it is only through such efforts that one can make an appraisal of the movement and the important point to bear in mind is that a statistical recital of progress is only a limited (and, possibly, unsatisfactory in particular cases) indicator of progress.

10·2 It is necessary to recognise that co-operation is both a means to better living and a system for moral upliftment. In a sense the two ends are interdependent for the one leads to the other and is, in turn, promoted by it. It has been of late fashionable for critics of the co-operative movement to harp unceasingly on the so called lack of the co-operative spirit amongst members of co-operative societies in India without always realising that true co-operative spirit cannot thrive in an atmosphere of sacrifice, for it is the outcome of successful economic enterprise. It would be desirable to recall the wise words of the Maclagan committee on co-operation[50] who stated as follows :—

> "The theory of Cooperation is very briefly that an isolated and powerless individual can by association with others and by moral development and mutual support obtain in his own degree the material advantages available to wealthy or powerful persons,

50 Report, para 2.

and thereby develop himself to the fullest extent of his natural abilities. By the union of forces material advancement is secured, and by united action self-reliance is fostered, and it is from the interaction of these influences that it is hoped to attain the effective realization of the higher and more prosperous standard of life which has been characterised as 'better business, better farming and better living'. We have found that there is a tendency not only among the outside public but also among supporters of the movement to belittle its moral aspect and to regard this as superfluous idealism. Co-operation in actual practice must often fall far short of the standards aimed at, and details inconsistent with co-operative ideals have often to be accepted in the hope that they may lead to better things."

Appraisal of the movement must bear these wise words in mind, and, while statistical recital of progress may indicate its outward growth, one must constantly recognise the need to continuously improve the quality of the people affected by the movement and strive unceasingly for the removal of those defects and shortcomings which tend to deviate the movement from its true goals.

10·3 Since the credit aspect of the movement is the most significant one in India, progress of primary agricultural societies must naturally constitute the first test of progress. The following table gives the development in this respect.

Primary agricultural Societies

Year	Societies (numbers)	Membership (numbers in millions)	Short and medium term advances (Rs. crores)
1950—51	104998	4·4	22·9
1955—56	159939	7·8	49·6
1958—59	182905	11·9	125·5
1960—61	210000	17·0	200·0

The above figures reveal substantial quantitative progress but apparently all was not well with the movement for

(a) overdues constituted 21 percent of the outstandings on 30th June 1960 as against 20 percent at the end of 1958-59,

(b) as many as 21,305 societies were dormant for 1 year and 22,594 for 2 years and more,

(c) the number of villages covered by dormant societies was as much as 56,411.

Some further idea of the agricutural credit societies can be got from the statement given below :-

Agricultural Credit Societies
(All-India Averages)

Item	Amounts in Rs. 1958-59	Amounts in Rs. 1959-60
1. Membership per society	65	71
2. Working capital per society	9,346	11,011
3. Share capital		
(a) per society	2,033	2,312
(b) per member	31	32
4. Deposits		
(a) per society	540	585
(b) per member	8	9
5. Loans advanced per member	105	117

It is apparent that as sources of thrift promotion the societies have not achieved much for neither share capital nor deposits* per member shows any significant improvement while the major portion of the increased working capital only reflected increased borrowings from State or Central co-operative banks. Again, while profitability is not the primary criterion of a good co-operative society, it still is an important index for no society run on uneconomic lines can in the long run either promote a co-operative spirit or command the loyalty of its members. Further, any successful cooperative credit society must be judged by the important test of prompt repayment of dues for it is in the avoidance of overdues that the development of the true co-operative spirit finds fullest expression. The following table gives interesting light on these aspects :-

* See Vol I. Ch. 1, Para 25, Table 14.

States	Proportion of Societiesloss working at a (1959-60)	Overdues as proportion of out standings (as on June 30, 1960)
Andhra Pradesh	27	14
Assam	34	55
Bihar	37	55
Gujarat	33	25
Maharashtra	21	27
Jammu & Kashmir	9	26
Kerala	34	20
Madhya Pradesh	16	21
Madras	24	11
Mysore	25	33
Orissa	35	20
Punjab	18	26
Rajasthan	13	19
Uttar Pradesh	10	6
West Bengal	27	43

Comment on the evidence revealed by the above table is hardly necessary for it is obvious that the credit movement, except perhaps in Andhra Pradesh, Madras and Uttar Pradesh, is running on its own overdues and a calamity or a crash is not far off.

10·4 The non-agricultural credit societies constitute that part of the movement which caters to the banking and credit needs of the small-income citizen living in urban and semi-urban areas. These societies serve the requirements of artisans, traders, factory workers and salaried employees. These societies are very popular in Punjab and Maharashtra which have nearly 33 percent of the total number of societies. At the end of the year June, 1960 the loans outstanding amounted to Rs. 106·52 crores and overdues at Rs. 7·76 crores formed 7·3 percent of this amount. However, these societies seem to have sponsored thrift for deposits held by these societies increased from Rs. 75·81 crores at the end of 1958-59 to Rs. 83·27 crores at the end of 1959-60, the societies in

Maharashtra and West Bengal accounting for 60 percent of the total deposits.

10·5 Agricultural marketing societies are generally classified into two types :

(a) State and Regional Marketing Societies.

(b) Primary Marketing Societies,

As regards the former the position is that while societies at the apex level have larger membership of societies, those at the intermediate level have larger number of individuals as members. However, the contribution made by these societies in the form of loans advanced and sales effected, though increasing from year to year, were insignificant in their total contribution to the economy of the country. The Primary Marketing Societies have, on the other hand, made good progress as would be clear from the table given below :

(Items 3 to 9 in Rs. crores)

Item	1958-59	1959-60
1. Number	2,380	2,501
2. Membership	9,68,239	11,83,907
3. Share capital	3·69	4·94
4. Reserves	2·25	2·60
5. Borrowings	8·53	11·04
6. Working capital	14·47	18·58
7. Loans advanced	12·20	15·87
8. Purchase	15·60	30·27
9. Sales		
(a) as owners	9·83	21·12
(b) as agents	16·88	25·52

10·6 We have seen that an important recent development has been the emergence of the concept of State partnership in the co-operative movement through assistance given by State Governments in the form of contribution to the share capital of different types of co-operative institutions. At the end of June 1960, the total contribution of State Governments towards such share capital amounted to Rs. 23·71 crores. The major portion of this amount was made available to primary agricultural societies who got Rs. 15·37 crores *i.e.* nearly 47 percent. The amounts made available to State Co-operative Banks and Central Co-operative Banks were much smaller, being only Rs. 5·62 crores and Rs. 8·77

crores respectively. The table given below indicates the relative position of Government contribution and the paid-up capital of the societies themselves :

(In thousands of Rupees)

States	Government contribution to share capital	Share capital paid-up
Andhra Pradesh	3,75,54	17,21,16
Assam	96,61	2,04,50
Bihar	1,54,59	4,19,54
Gujarat	3,21,73	19,48,61
Jammu & Kashmir	17,76	57,06
Kerala	84,06	4,52,74
Madhya Pradesh	2,58,13	8,60,67
Madras	2,80,32	17,24,51
Maharashtra	5,62,13	42,33,97
Mysore	2,72,53	14,56,53
Orissa	1,03,10	3,67,83
Punjab	2,47,18	12,91,42
Rajasthan	75,71	4,59,62
Uttar Pradesh	3,49,62	23,06,16
West Bengal	42,21	8,12,10

It is obvious that no specific relationship between the two exists so that in some cases, as for instance in Kerala, West Bengal and Rajasthan the contribution of the Government is small compared to the paid-up share capital, while in certain other cases, as for instance in Bihar, Madhya Pradesh and Orissa it is very large comparativly. The basic considerations affecting this question has been discussed earlier ; it may however, be added that lack of an uniform policy in this respect may imply infiltration of an element of variation in the co-opertive movement from State to State which may be undesirable.

10·7 The present position of the Co-operative Movement in India is indicated in the table given on next page ;

Co-operative year July 1959-June 1960.
(Amounts in lakhs of rupees)

Type of Society	Number	Membership (in thousands)	Working capital	Loans advanced	Value of goods Received or produced	Value of goods Sold
I All Societies	3,13,499	3,12,71	1083,47	325,32*	273,05	388,45
II Credit Societies						
(A) Short-term						
1. State Banks	22	31	174,74	196,92	—	—
2. Central Banks	400	3,69	247,40	297,14	—	—
3. Primary Societies						
(a) agricultural	2,03,172	1,44,23	223,70	169,09	43,31	33,30
(b) grain banks	9,554	12,13	4,41	1,47	—	—
(c) non-agricultural	11,371	42,31	137,40	117,40	7,02	5,63
(B) Long-term						
1. Central Land Mortgage Banks	16	2,17	37,38	8,52	—	—
2. Primary Land Mortgage Banks	408	5,50	20,39	5,10	—	—
III Non-credit	88,556	1,02,37	238,05	44,21	222,72	349,52

* Primary Societies Source—Reserve Bank.

The preponderance of agricultural credit societies in the movement is apparent and in spite of more than fifty years having elapsed since its introduction, the credit-aspect continues to be the mainstay of the work done. This is, of course, not surprising considering the nature and characteristic of the Indian economy, and it is, therefore, not unusual that nearly 65 percent of all societies were agricultural credit societies. There was a sudden spurt of expansion in 1959-60 when membership increased by 22·2 percent compared to the

previous year. It has been calculated that "assuming an average family comprises five members, it may be estimated that by the end of 1959-60 roughly 1515 lakhs or about 38 percent of the population was served by co-operatives compared to 1240 lakhs or a little more than 30 percent at the commencement of the year. Allowance will, however, have to be made for individuals being members of more than one society."[51]

The Third Five Year Plan envisages an enormous expansion in the co-operative movement. It targets for a coverage of about 60 percent of the agricultural population through the movement with a total number of societies of not less than 230,000 so as to serve all the villages in the country. While one would hardly deny the need for spreading the co-operative movement further, one may wonder whether the target of a very rapid expansion may not lead to a sacrifice of quality for formation of co-operatives should never be pressed further or faster than what the people want for, after all, it is their organisation.

11. Concluding Remarks.

11·1 The development of the co-operative movement has been uneven in the different States. The table given below shows the extreme variations in the position from State to State :—

State	Percentage of Co-operative Societies (1958-59)	Percentage of Primary Society membership (1958-59)	Population (1961)
Andhra Pradesh	7·7	11·3	8·2
Assam	2·1	3·2	2·7
Bihar	9·2	3·6	10·6
Gujarat	3·9	6·0	4·7
Jammu & Kashmir	0·7	1·2	0·8
Kerala	2·1	4·8	3·8
Madhya Pradesh	8·2	4·0	7·4
Madras	5·3	12·9	7·7
Maharastra	8·3	11·3	9·0
Mysore	4·2	7·3	5·4
Orissa	3·5	4·0	4·0
Punjab	9·7	6·0	4·6
Rajasthan	3·9	2·4	4·6
U.P.	20·8	13·3	16·9
West Bengal	7·0	7·7	8·0
INDIA (including Union Territories)	(100)	(100)	(100)

51. Reserve Bank—Statistical Statements Relating to the Co-operative Movement in India, para 7.

It is obvious that the percentage of population covered by the membership of primary co-operative societies is neither uniform nor does it bear any appropriate relationship either to the number of societies or to population of the State. The problem of assessment is intimately concerned with finding out the reasons why the movement has developed more in one State rather than in another. The scope for and rate of development of co-operatives is influenced by :

(a) prior level of development,

(b) non-official leadership and effort,

(c) official imaginativeness and vision,

(d) flexibility of rules and procedures,

(e) nature of the economy *i.e.* agricultural or industrial,

(f) level of living *i.e.* savings and assets available, and

(g) land ownership patterns and the distribution of land holdings.*

It is also necessary to recognise that general social and economic development exert an important influence on the co-operative sector even when not directly included in its purview. Thus, even on *a priori* reasoning one must admit that pattern of land ownership, and, the nature and scope of land reforms legislation and its impact on the pattern of land rights would have significant infiuences on the co-operative movement, particularly its agricultural credit side. In actual practice also it has been found that absence of intermediary right holders and the *Ryotwari* tenure is conducive to the better development of co-operatives. Further, social conditions in India being what they are, big land-holders naturally dominate local credit co-operative societies. From this point of view one may expect effective operation of land-ceilings to stimulate the growth of co-operatives.

11·2 The nature and type of the State's economy must naturally affect the development of the movement. An area subject to uncertainties and natural calamities must show a slower rate of progress than another, where due to widespread and well-organised irrigation, which has a stable economy. Further, the growth of non-credit activities like marketing depend on the extent of monetization and commercialization, and both credit and non-credit activities are restricted in their development in a subsistence economy. Thus, States with larger numbers of uneconomic or subsistence holdings and with greater proportion of self-consumption of produce raised must naturally have a more limited growth of co-operatives.

* See Vol. I, Ch. 1, para 4.

11·3 In a country where the movement has always been sponsored by the State and is continuously looked after by a specialised Co-operative Department with a high power officer as Registrar, the efficacy of the department is in a sense the most significant factor in securing the development of the movement. The following comments from the General Review Report[52] of the Reserve Bank's Follow-up Survey (1956-57) are of interest :—

(a) In regard to State partnership in Share Capital "the targets fixed were not achieved",

(b) "In regard to State partnership in management, the steps taken by the Co-operation Departments were very inadequate",

(c) "As regards the co-operative development plans and their implementation, not always was adequate attention paid by the Co-operation Departments in selecting societies for conversion into large size ones or for sanctioning loans and subsidies for construction of godowns or for appointment of managerial staff",

(d) "......there was no uniform policy for selecting institutions at the primary level for State partnership. For instance, some of the societies which were converted into or amalgamated to form large size societies had heavy overdues or cases of misappropriation and embezzlement were pending, with the result that they did not have a proper start",

(e) "In regard to the general guidance extended by the Co-operation Department,......it was sometimes inadequate". Some of the important aspects such as the linking of credit and marketing, demarcation of the jurisdiction and functions of different types of societies, enunciation of the rights and duties of the State nominees, reorientation of loan policies of the central banks, rationalization of loan procedures etc. "did not receive adequate attention",

(f) "Speedy action was sometimes lacking in regard to liquidation, arbitration and execution of awards. This resulted in heavy overdues and in the continuance of dormant societies, both of which features adversely affected the growth of co-operative credit".

52. Ch. 20, See 20.8.

V

INDUSTRIAL LABOUR AND TRADE UNIONISM

1. Nature and Characteristics of Industrial Labour.

1·1 Industrial development must bring along with it the growth of a sector of the population that depends for its economic prosperity on employment in the organised industries. In every country of the world, growth of industries has always led to the growth of an "employee" class who are not directly interested in industrial profits but whose earnings and aggregate volume of employment* depend on the volume of industrial production, which, in turn, at least in the private sector, is predominantly influenced by the profits of the entrepreneur. Of course, the link between the extent of industrial profits and the volume of industrial employment and its earnings is essentially a long period phenomenon ; but except where, as for instance in the public sector, volume of production and employment is allowed to remain unaffected even when there is a decline in the profits of the undertaking, the fortunes of the industrial labour population must be intimately connected with the fortunes of the industry.

1·2 Growth of industries in a country is usually reflected in the rising number of factories, but a more correct approach would be to judge the trends revealed by the Index of Industrial Production. The table given on the next page brings out how with expanding industrial production, the volume of employment in the country has also shown steady growth.

It must, however, be recognised that comparison of employment levels from year to year are difficult in India because of lack of comparability in the figures due to changes in classification and also because of lack of reliability in the figures supplied. Even allowing for such limitations, one can see a fairly close correspondence in the growth of employment and growth of production, particularly for the private sector.

* See Vol. I, Ch. I, pp. 59-61. and Ch. VI, pp. 234-36.

Year	Index of Industrial		Average daily employment in factories	
	Production	Profits	Public Sector	Private Sector
(1)	(2)	(3)	(4)	(5)
1952	103·6	99·0	326,254	2,241,199
1956	132·6	165·0	361,024	2,521,285
1957	137·3	151·7	428,799	2,938,328
1959	151·9	168·7	481,937	2,993,977

N.B. 1. Index of Industrial Production Base 1951 = 100.

2. Index of Industrial Profits Base 1950 = 100. Figures represent Gross Profits including depreciation; for 1959, figures for 1958 used.

3. For the concept of Index of Industrial Production see Vol. I, Ch. VI, para 2·2·2.

4. For details of the Index of Industrial Profits. see Vol. I, Ch.VI para 3.2.4.

5. In accordance with the unfortunate (statistical) tendency in India, the base for the Index of Industrial Profits has recently been shifted to 1955 making subsequent figures incomparable. The figures of the new index are naturally lower than those of the old index for years subsequent to 1955.

1·3 Normally one would expect that for a country with a large and increasing population suffering from a high pressure on land there would be an abundant supply of labour for industries. There is, however, a certain scarcity of skilled labour in India and the supply of unskilled labour has also not been always adequate to the demand in all areas though undoubtedly the overall supply of unskilled labour has generally been in excess of demand. The two characteristics of Indian Industrial Labour which have generally adversely affected its supply are

(a) its migratory character, and

(b) its heterogeneous composition.

It is well known that the factory operatives in India are mostly drawn from the villages who are always eager to go back to their homes, especially during the busy agricultural season. In a sense the factory workers in India are 'pushed' to the industrial area because of lack of employment in the villages for it is doubtful whether even now the majority of the workers would prefer employment in factories if they could get a reasonable income from land or from occupations in villages. The migratory character of labour causes a constant change in labour turnover and leads to an aggregate loss of efficiency due to frequent changes of jobs and inflow of new persons not adequately acquainted with work in the factory.

In recent times, however, a change has been noticeable, and, with the development of rapid communication the time is not far off when, as in the west, a labour force would grow that would live permanently in towns with perhaps an occasional visit to their villages for short holidays. The different areas from which the labour force is drawn again is a serious disadvantage that contributes to inefficiency. There is a lack of linguistic unity and an absence of community of interests, both of which create special problems in industrial areas. Further, the heterogeneous composition of the labour force makes canteen and housing facilities difficult, leads to more frequent absenteeism in the aggregate and, above all, creates a lack of cohesion amongst the workers which is neither helpful to themselves nor useful to the employers.

2. Industrial Efficiency and Indian Labour.

2·1 Efficiency of labour is an important factor both for industrial progress and for improving export potentiality. Generally labour-costs are a substantial factor in total cost of production and unless labour is efficient, competitive power of Indian industries must be adversely affected in the international market. Even internally, high costs lead to high prices which restrict demand and react unfavourably on volume of production. It is not denied that overall efficiency of production is essential; but it is equally true that efficiency of labour is perhaps the primary factor in overall efficiency. It is, of course, difficult to have a precise measure of efficiency for comparisons of physical output in relation to given units of time may often be misleading while comparisons of value of output in relation to money remuneration paid may be illusory. There is a commonly prevalent idea that Indian labour is comparatively less efficient, though the Labour Investigation Committee of 1946 observed that "the alleged inefficiency of the Indian worker is largely a myth. Granting more or less identical conditions of work, wages, efficiency of management and mechanical equipment in the factory, the efficiency of the Indian labour generally is no less than that of workers in most countries." In short, while there are certainly factors that at present tend to make the Indian labour's efficiency low, there is no reason to believe that any racial or climatic causes underlie such lack of efficiency, so that if appropriate steps are taken there is no reason why Indian labour should not be as efficient as labour in the most industrially advanced countries of the world.

2·2 Broadly speaking efficiency of labour is the outcome of four main factors, *viz.*,

(i) Inborn quality,

(ii) Health and Strength,

(iii) Intensity of effort put in, and

(iv) Acquired skill.

Of the above, the first one apparently is something which cannot be influenced by external factors ; but the other three are the result of a totality of environment in which the earnings of labour constitute a significant factor. It is a truism that an adequate wage-level ensures a decent standard of living which in turn improves efficiency by raising health and strength, introducing an urge to more intensive work, and, facilitating acquisition of skill and obtaining of technical training. It has, therefore, been rightly argued that "If exploitation is prevented and wages are forced up to a fair level, the benefit to efficiency will start an upward movement. ....High earnings will lead to the greater efficiency ; greater efficiency will lead to the power of obtaining higher earnings, both because the workers' services are worth more and because, being better off, they are in a stronger position for bargaining ; the higher earnings so obtained will react again to increase efficiency ; and so on cumulatively."[53] There is reason to believe that the factory worker in India has of late had a set back in his real earnings.* It would, therefore, appear not unreasonable to hold that a rise in wages would have favourable reactions on efficiency, and, that these reactions would be more favourable if such rises are specifically achieved for

(a) work people who are exceedingly poor, and in whom, therefore, there is large scope for physical improvement through better food, clothing and house accommodation,

(b) occupations where employment is fairly regular so that a definite standard of life can be built up, and

(c) periods which are fairly long and continuous so that there are greater chances of efficiency being favourably benefited appreciably.[54]

It seems, therefore, that if adequate steps could be taken to raise the real earnings of factory labour in India, a major step would have been taken to improve the efficiency of labour in India apart from providing an incentive to additional effort.

53. Pigou—Economics of Welfare p. 550.

* Vol. I, Ch. VI, para 7.

54. Pigou—Ibid p. 549.

3. Factory Legislation and Social Welfare.

3·1 Next in importance to the earnings of labour, the working conditions in factories constitute a significant factor in determining the efficiency of labour. The various Factory Acts represent the steps taken by the State to improve the conditions under which workers carry on their work and ensure protection from danger by improving safety arrangements. The main purposes of these legislations have been to regulate and improve

(i) sanitary conditions, adequacy of space and appropriate ventilation arrangements ;

(ii) arrangements for safety and prevention of accidents ;

(iii) hours of work, intervels and days of rest ; and

(iv) the especial conditions of employment in mines, plantations and railways.

Factory legislation in India dates back to as early as the Factory Act of 1881 which prescribed modestly the age of 7 years as the minimum age of employment and prescribed a maximum of a 9 hour a day for labour between the ages of 7 and 12. Subsequent legislation has continuously expanded the scope of regulation until the Factory Act of 1934 prescribed maximum hours of work for adults. The history of factory legislation in India has been mainly a history of continuous improvement and greater conformity to international standards, especially in the matter of prohibition of employment of child labour, engagement of women labour particularly in mines and other dangerous occupations, and, laying down maximum hours of work per day and per week.

3·2 Broadly speaking, legislative measures relating to employment conditions in India may be classified into :

(a) Specific legislation relating to particular industries like manufacturing, plantations, mines, transport or shops ; and

(b) General labour legislation dealing with such issues as abolition of servile labour, social welfare, social insurance, maternity benefit, workmens compensation, trade disputes etc.

Generally, all specific legislation attempted to improve the health and strength of the workers by preventing unhygenic conditions of work and by prohibiting long hours of employment as it is an acknowledged fact that efficiency is adversely affected by these factors. It is a sad reflection

on the private sector that the Rege Committee (*Vide* p. 144 of its Report) found it necessary to assert that "In regard to working conditions most of the employers rarely do more than what they are forced to do by laws and even this is evaded in several cases."

3·3 *Social Security and Labour Welfare.*—It has been universally recognised that the modern economic system introduces certain elements of uncertainty and various sources of evil against which organised provision for social security is essential. Such provision is consequent on the recognition that there do exist contingencies against which the individual, especially the recipient of a small contractual income, could not be expected to effectively provide by his own ability. In some cases individuals may, on their own initiative, attempt to combat some of these evils through cooperative effort as for instance through co-operative health schemes or pooled sickness benefits. Generally, however, modern welfare states are required to promulgate security measures and provide for social services. Recent efforts in India have been directed towards provision of a form of partial security through the Employees State Insurance Act of 1948 which conferred the following essential benefits :

(i) Sickness,
(ii) Maternity,
(iii) Disablement,
(iv) Dependant, and
(v) Medical.

The scheme is based on the principle of mutual sharing, loosely on the criterion of ability, through contributions from State funds in the form of grants and donations and by the employees as well as employers. The administration of the scheme is under an autonomous body called the Employees State Insurance Corporation. In the initial stages the operation of the scheme was confined to a few selected industrial centres but it has been steadily extended so that by the end of the Second Plan period it has been implemented in more than 100 centres and has brought under cover about 17 lakh industrial workers. The scheme is expected to be further extended during the Third Plan period so as to bring about a coverage of about 30 lakh workers. All centres having a concentration of five hundred or more industrial workers would be covered by 1966. In addition, the Employees' Provident Fund Scheme, introduced in 1952 to ensure compulsory contribution to a provident fund

arrangement by both employers and workers, is to be considerably extended during the Third Plan period. Under the present scheme every worker who has completed one year's continuous service and whose basic wage does not exceed Rs. 500/- per month is compulsorily incorporated in the scheme with a 6¼ percent contribution from both employers and employee. The scheme is intended to provide a sort of saving to be available on retirement either on attaining the age of 55 years or on account of incapacity for work. The proposal to enhance the rate of contribution from 6¼ percent to 8⅓ percent, though accepted in principle, is being further studied to enable assessment of industries not capable of bearing the additional burden so that if necessary, differential adjustments to the extent required may be considered.

3·4 It is being increasingly recognised that piecemeal measures to combat social evils should be replaced by an integrated scheme of social security not only to secure greater efficiency and economy, but also to achieve coordination of developmental planning with social security programme. It may be pointed out that a study group on Social Security had recommended "the integration of existing social security schemes and the conversion of the various provident fund schemes into a statutory scheme for old age, invalidity and survivorship pension-*cum*-gratuity."[55] This group, known commonly as the V. K. Menon Study Group, made the following important suggestions :

(a) setting up of a central organization to administer the Employees' State Insurance Scheme and the Employees' Provident Fund Scheme after amalgamation of the two,

(b) The liability of employers in respect of gratuities should be made statutory and the employees should be required to pay this as contribution towards a pension-*cum*-gratuity scheme, and

(c) the provident fund be converted into a statutory pension scheme.

These recommendations were made in 1958. They were fully endorsed by the 1958 Labour Ministers' Conference. It is recognised universally that a developmental planning programme must necessarily have an important welfare bias which can be fully achieved only through a comprehensive social security system ; and yet, the Third Five Year Plan[56] merely contents itself by stating that "urgent consideration has now to be given to the various aspects of

55. Third Five Year Plan, p. 257.
56. Chapter XV, para 25.

the question of integration, so that the entire scheme takes shape as early as possible".

4. Labour Welfare and the Third Five Year Plan.

4·1 The policy adopted in recent times by Government has been directed towards a threefold objective, *viz.*

(i) securing minimum wages,

(ii) improving working conditions and social security

(iii) expanding training facilities.

In regard to the first one, the responsibility assumed so far is only selective and is intended towards "securing a minimum wage for certain sections of workers, in industry and agriculture, who are economically weak and stand in need of protection."[57] The instrument for securing this benefit is the Minimum Wages Act of 1948, subsequently amended in 1957, which provides for

(a) fixing minimum wages in employments where exploitation through sweated labour may be prevalent,

(b) fixing guaranteed and minimum time-rate, minimum piece-rate and an appropriate overtime-rate,

(c) appointment of committees to hold enquiries and advise in fixing the rates of minimum wages.

The concept of the minimum wage-rate envisaged in the Act was to secure either a basic minimum rate of wage with a cost of living allowance or a basic rate with or without a cost of living allowance and the cash value of the concessions in respect of supplies of essential commodities at less than market price rates. An interesting feature of the Act is that it recognises the possibility of payment of wages in kind, wholly or partly, and empowers the appropriate governments accordingly.

4·2 It must be frankly admitted that measures for fixation and revision of wages have not proved very effective, mainly because of an inadequate machinery for inspection and enforcement. However, even with limited enforcement it is likely that such an enactment must over time prevent the exploitation of labour by strengthening the hands of employers willing and able to pay for workpeople's services as against the unfair competition of employers working with "sweated" labour. It is, of course, difficult to conceive of a national minimum wage for a country like India where

57. Third Five Year Plan p. 256.

not only is there wide diversity as between industry and industry but there also exists wide divergence of productive conditions even in the same industry located in different areas. Some idea of this diversity can be got by comparing the average per capita annual earnings of factory workers in the different states given below :-

(In Rs.)

States	1956	1957	1958
Andhra Pradesh	595	1031	709
Assam	1526	1833	1223
Bihar	1236	1299	1283
Bombay	1415	1453	1459
Kerala	736	805	...
Madhya Pradesh	982	1139	1217
Madras	950	979	...
Mysore	853	968	...
Orissa	949	957	981
Punjab	991	955	1217
Rajasthan	770	907	942
Uttar Pradesh	1014	1078	1099
West Bengal	1142	1174	1179
All India	1187	1234	1282

N.B. Figure rounded for convenience.
Source : Labour Bureau.

The divergence of per worker earnings (annual averages) of factory labour from industry to industry is illustrated below with reference to certain selected industries.

Annual Averages of Per Worker Earnings

(Rs. per worker)

Year	Textiles	Paper and paper products	Basic metal industries	Miscellaneous Industries	All Industries
1951	1,044·0	957·9	1368·2	1067·3	1035·6
1955	1,191·3	1062·5	1673·4	1209·8	1173·5
1958	1,305·5	1226·4	1557·3	1220·0	1295·2
1959	1,358·7	1313·9	1531·8	1258·9	1333·3

N.B : For details see C.S.O.—Annual Abstract of Statistics.

From the above it is obvious that any search for an uniform national minimum wages is a search for a non-existent illusion, and, practically speaking, the best solution would be the setting up of Wage Boards, preferably of a permanent nature, to deal with wage disputes in each industry in each State.

4·3 *Fair Wages and Profit-Sharing.* Under conditions of competition, the play of economic forces tends to secure over time more or less stable conditions under which in industries in general there is a rough correspondence between the value of the marginal net product of labour and wages. Broadly speaking such correspondence between the two depicts that wages are "fair", and, it could be reasonably argued that if workers were to receive less, there would be a lack of inducement which would adversely affect industrial efficiency. In a progressive economy conditions are continuously changing that tend to bring about a rise in the money value of the marginal net product of labour and making old fair rates of wages low. A study of the productivity of labour, therefore, is an important question, for without such a study no proper assessment of the concept of fair wages would be possible, especially when inflationary trends, advances in techniques and use of modernised equipment, and, planned development of new industries are all tending to increase the money-value of labour-productivity. In a money-economy all productive effort must, in the ultimate analysis, be measured in terms of value. It has been estimated[58] that

(a) "the value added per worker as well as per person has been showing a perceptible rising trend", and

(b) "the value added as percentage of wages of workers has been relatively more stable.',

A table constructed on the basis of C.M.I data gives the following results :

(Biennial averages in Rs.)

	1950-51	1954-55	1956-57
Value added per worker	2,142	2,542	2,792
Value added as percentage of wages of workers	217·7	229·2	239·0

N.B. : For details see C. S. O. Monthly Abstract of Statistics, October 1960, p. XV.

A comparison of the rate of growth of the two would bring out that perhaps the workers have not received an adequate increase in their wages proportionate to the increase in the value added per worker. However, the broad principles of wage determination have been laid down in the

58. S. G. Rao—Productivity—A Value Aspect in C.S.O. Monthly Abstract of Statistics, October 19C0.

Report of the Fair Wages Committee which attempted to indicate the content of the needbased minimum wage that would also provide for the acquisition and development of skills and for improvements in output and quality. To quote the words of the committee :

> "We consider that a minimum wage must provide not merely a bare sustenance of life but for the preservation of the efficiency of the worker. There should be a provision for fair wage which should be fixed somewhere between minimum wage and living wage."

In short, the underlying idea of a fair wage is an approach to a sort of living wage providing for a higher level of living than a minimum wage could provide. Thus, according to the committee's concept of fair wages, provision should be made not only for the minimum standard of living but also for education, protection against ill-health and requirements of essential social needs.* It is unfortunate that the Fair Wages Bill of 1950 was allowed to lapse and no efforts have been made to revive it, especially as the recognition of the principle of a worker's *right* to a fair wage is logically implicit in any welfare policy which aims at achieving rising real wages as the basis for an improved level of living. Intimately connected with the concept of fair wages is the concept of profit sharing for the two taken together constitutes the worker's direct share from the national dividend. In fact, the Industries Conference of 1947 recognised the need for evolving some sort of partnership between labour and the employer in the interests of securing industrial peace and inducing increased production. The Expert Committee on Profit-Sharing (1948) outlined the basic policy as follows :—

(a) A fair wage to labour must be the first charge on industrial production ; or, in other words if labour is engaged, it must be paid a living wage irrespective of whether profits are made or not. This proposition is only a recognition of the fundamental peculiarity that labour, even when used as an agent of production, is ultimately a part of the consuming population which is the end of all productive effort.

(b) After a fair wage is paid, adequate provision should be made for other legitimate charges on receipts from sale of output, and, any excess of profits left

* See Vol. I, Ch. III pages 113-115.

> after allowing for depreciation, expansion and a fair return on capital employed should be available for sharing with labour as additional remuneration. This additional share, according to the committee, should bear a definite relation to production.

It is obvious that the first proposition is unexceptionable, especially in a country where the socialistic pattern of society has been adopted as the basic ideal of planning.* The second proposition, however, is likely to be a source of controversy for no objective and undisputed norm for assessing the allowance to be made for this is readily available. The appointment in 1960 of a Commission to go into the question of bonus and to evolve norms for its payment is an indication that this might lead to the evolving of a satisfactory solution to the controversial question of profit-sharing since any proper scheme of bonus payment must necessarily be linked to profits and be a part of a wider scheme of profit-sharing.

4·4 The average annual earnings of factory employees during the last decade has shown substantial increases.† This would be evident from the table given below :

Index of Gross Industrial Profit Base 1950=100	Year	Average annual earnings (Rs.)	Index Base 1950=100
(1)	(2)	(3)	(4)
100	1950	966·8	100·0
99·0	1952	1112 2	115·0
125·1	1954	1111·3	114·9
165·0	1956	1208·1	125·0
151·7	1957	1233·9	127·6
168·7	1958	1282·4	134·0

During the same period, the Index of Gross Industrial Profits (including depreciation) rose from 100 in 1950 to 168·7 in 1958, so that in a sense the earnings of labour did not rise *pari passu* with the rise of industrial profits.** It is, however, possible that partly at least the rise in profits represented the conjunctural effects of inflationary trends and should not, therefore, be logically a proper basis of profit-sharing for labour. As the Third Five Year Plan[59] rightly emphasises :

* See Vol. I, pp. 4-6, 445-447.

† See Vol. I, pp. 245-246.

** The new Index with 1955 base naturally shows lower rise.

59. Ch. XV, para 37.

"Industry is being called upon to meet, as rapidly as possible, the claims on behalf of the workers for a living wage, better living and working conditions, the needed volume of employment opportunities and a fuller measure of social security. It must yield a reasonable return on capital and provide for capital formation on an adequate scale. Neither the exercise of their organised strength in industrial conflicts, nor laws and the intervention of the State can help the workers much in realising their aspirations. Their gains can arise only out of the strength and dynamism of the economy, the only enduring basis of which is a rising level of productivity. No increase in profits which does not come out of improvements in productivity but has its origin in current scarcity and the stresses of development can be regarded as a sign of prosperity."

5. Trade Unionism and Industrial Relations.

5 1 A significant feature of industrial development is the growth of organised labour and collective bargaining, which in its turn leads to trade disputes and violations of industrial peace. While the loss to the economy and national income from such industrial disputes may sometimes be considerable, such loss, by itself, cannot be an argument for curtailing the rights of labour to organised action in self-interest, especially if there are reasons to believe that labour has not received its due share of increased economic prosperity brought about through national planning.[60] A modern economic system is a highly integrated organisation and the loss from labour and equipment rendered idle by a strike or lockout is not only confined to the industry itself but extends directly and indirectly to the aggregate national dividend in the following ways :

(i) it reduces aggregate consumer expenditure and hence curtails the demand for the goods of other industries by reducing the earnings of the people actually involved in the dispute, and

(ii) it adversely affects production in related industries which are either users of the products of the industry subject to the stoppage or suppliers to that industry.

Thus any industrial dispute must inflict an injury, both direct as well as indirect, on the national dividend ; though as Pigou has pointed out that

60. For a policy statement on Disparities of Income, See Third Five Year Plan Ch. I, paras 50-54.

"........the net contraction of output consequent upon industrial disputes is generally smaller than the immediate contraction; for a stoppage of work at one place may lead both to more work at the same time in rival establishments and to more work at a later time (in fulfilling delayed orders) in the establishments where the stoppage has occurred."

This, however, only emphasises that the economic system struggles to reduce the evils of industrial disputes, though they remain evils and are sources of economic loss to the community.

5·2 Some idea of the economic loss following from industrial disputes can be got from the table given below :

	Year	Stoppages	Number of Workers involved	Man-days lost
Monthly Average	1955	97	43,981	474,821
,,	1958	127	77,381	649,799
,,	1960	130	81,905	542,913
,,	1961	113	35,915	253,543
May	1961	121	31,860	335,838
Oct.	1961	138	60,210	342,218

N.B. : 1961 figure average of ten months, January to October.

The economic loss arising from such disputes is obviously fairly significant for a country engaged in planning which must seek to remedy such losses, and, labour policy in a planned economy must be suited to the needs of such an economy. The principles and practices that have grown up in the country recently are the result of joint consultations between Government, labour and employers and much of the national policy has been operating on a voluntary basis with Government assuming powers of intervention.

5·3 The earlier approach before the Second Five Year Plan was based on the idea of conciliations, with measures available to the State to refer unresolved disputes to tribunals set up for the purpose. It was normal to regard such a reference as making the dispute *sub judice* so that stoppage of work after such a reference were declared illegal. Similarly contravention of awards and agreements were also treated as illegal. This approach proved to be a mixed blessing, for

the system

> ".........has helped to check the growth of industrial unrest and has brought for the working class a measure of advance and a sense of security which could not otherwise have been achieved. At the same time, the spirit of litigation grew and delays attendant on legal processes gave rise to widespread dissatisfaction."[61]

5·4·1 Trade unionism in India has been comparatively of recent origin as it was only with the passing of the Trade Unions Act of 1926 that legalised development of the movement was possible. Upto 1947, Trade Unions were more like 'strike committees' with an isolated existence for each industrial unit and there was little of what may be called Trade Unionism in the wider sense of an association of labourers for promoting common labour interest. The Indian Trade Union Amendment Act, 1947, however, gave a fillip to the movement by providing for compulsory recognition of representative unions by the employers. The Act further provided for the appointment of Labour Courts to consider disputes arising from the refusal of employers to recognise any particular union. In 1950, an attempt was made to consolidate and modernise legislation relating to Trade Unions, and a Bill was introduced in Lok Sabha. This Bill had many redeeming features and provided for

(i) compulsory registration,
(ii) compulsory recognition by employers,
(iii) admission of outsiders for making the organization broad-based, and
(iv) a code of conduct for improving the tone of labour-management relations.

Enactment of the provisions of the Bill had to be postponed due to severe opposition in Parliament and subsequently neither this Bill nor the Industrial Relations Bill of 1950 has been revived. This is partly obviously due to reluctance on the part of Government to revive controversial legislation but mainly because "In the course of the Second Five Year Plan a new approach was introduced to counteract the unhealthy trends and give a more positive orientation to industrial relations, based on moral rather than legal sanctions."[62]

5·4.2 The growth in the number of registered Trade Unions in India has been fairly rapid ; but membership rather than number of Unions is a more correct measure of the true

61. Third Five Year Plan, p. 250.
62. Third Five Year Plan, p. 250.

significance of the movement. Unfortunately, it is difficult to assess the growth in membership as many Unions do not furnish information in time. However, some idea of the growing importance of Trade Unionism in India can be got from the table given below :

Year/ State	No. of registered Trade Unions	No. of Unions furnishing information	Percentage of response	Membership of Unions furnishing information	Average Membership
(1)	(2)	(3)	(4)	(5)	(6)
1951-52	4623	2556	55·3	1,996,311	781
1956-57	8554	4399	51·4	2,376,762	541
1957-58	10,045	5520	55·0	3,015,052	546
1957-S8					
Andhra Pradesh	608	199	32·7	1,06,733	536
Assam	136	50	36·8	73,072	146
Bihar	544	407	74·8	318,139	782
Bombay	1685	1030	61·1	601,964	584
Kerala	1216	826	67·9	356,786	432
Madhya Pradesh	283	92	32·5	45,441	494
Madras	814	662	81·3	315,900	477
Mysore	408	201	49·3	107,548	535
Orissa	119	75	63·0	71,442	952
Punjab	406	217	53·4	60,995	281
Rajasthan	212	112	52·8	24,281	217
Uttar Pradesh	971	615	63·3	260,706	424
West Bengal	2324	785	33·8	472,755	602

Source : Labour Bureau.

In terms of absolute numbers, there has undoubtedly been fairly rapid progress; but relative to the total employment* in the Industrial Sector, it is doubtful whether the expansion of the movement has provided adequate coverage to the workers.

5·4·3 The growth of trade unionism depends as much if not more, on the nature of the working population as on the growth of organised industries. The very nature of our labour force provides a retarding influence and is responsible

* See Vol. I, p. 59, 100-107.

for many of the defects and weaknesses of our trade unions. The chief factors that prevent the growth of healthy trade unionism in India may be summed up as follows:—

(i) lack of a stable working population due to the migratory character of Indian labour,

(ii) lack of a surplus earning power over the minimum subsistence level that makes for paucity of funds for the unions,

(iii) the heterogeneous nature of the labour force, with its differences of languages, religion and culture make a united voice difficult, if not impossible,

(iv) uneducated and ill-educated labour that is unable to throw up real leaders from amongst themselves and this enables unscrupulous outsiders to often mislead the ignorant labourers, and

(v) inability of the unions to engage technically qualified and properly paid advisers and staff to continuously study the interests of labour and "brief" the managing committees properly.

5·5 An interesting question to consider is whether in the envisaged socialistic pattern of society, there is much desirable scope for collective bargaining by trade unions for raising wages in particular industries. It would appear rather anamolous to have strikes and lockouts for raising wages of particular groups of workers in a scheme of planning envisaged for achieving 'Social Justice'. The approach introduced during the Second Five Year Plan appears, therefore, more in harmony with the present objectives of planned economy in India. The new approach provides a more positive orientation to industrial relations and emphasises more the moral sanctions *vis a vis* legal sanctions. It strives to achieve prevention of unrest rather than *post facto* cure, and aims at removing root causes rather than superficial patching up of conflicting economic interests. A Code of Discipline in Industry has been developed through voluntary acceptance and the code is applicable both to the public and to the private sector. It lays down specific obligations intended to promote agreed efforts for securing industrial peace. The code seeks to develop measures on the part of both the management and the workers for avoiding stoppages and long drawn-out legal remedies by securing settlement of disputes and grievances by mutual negotiations, conciliation and voluntary arbitration, facilitating the free growth of trade unions and eliminating all forms of coercion and violence in industrial relations. Judged by results, the new

approach has apparently led to good results. To quote from the Third Five Year Plan[62]:-

> "It is obvious that a new concept with such far-reaching aims, in a difficult field, requires a considerable period of earnest endeavour before it gets firmly established in practice. The results so far achieved are, however, encouraging both in terms of the reduction of man-days lost owing to stoppages and in bringing about a general improvement in the climate of industrial relations. The number of man-days lost declined steadily and significantly from 47 lakhs during January-June 1958, the six months prior to the introduction of the code, to 19 lakhs during July-December, 1960. The code has also been successful in creating an awareness amongst the employers and workers of their obligations towards each other; the desire to settle disputes mutually without recourse to the wasteful methods of trial of strength and litigation is steadily growing."

6. Recent Trends in Labour Policy

6·1 *Joint Management Councils.* It has been generally felt that in a socialistic pattern of society, the workers must increasingly have a sense of 'belonging' and be progressively associated with management. It is fully recognised that a vast net-work of planned effort could hardly be expected to succeed unless all concerned in the productive effort were associated with it and had a feeling that they were helping to build a progressive State. Towards this end Joint Management Councils have been set up providing for workers' participation in management. The main function of these councils is to secure mutual consultation between workers and employers so as to assist in achieving industrial peace and further the objective of better industrial relations. Through such councils, the advantages likely to accrue are :

(i) increased productivity,

(ii) better working and living conditions,

(iii) greater awareness in the industry of its social obligations in a planned economy, and,

(iv) provision of a responsible channel of communication between labour and management which would help to remove the present unfortunate feeling that

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62 p 251

their interests must, in all issues, be divergent and contradictory.

Even though the experience of these Joint Management Councils have been so far extremely limited, there are encouraging indications that the results have been found to be satisfactory and heartening. The scope of the functions of these councils has been rather vaguely defined, so that variations from place to place and industry to industry are noticeable. This lack of definiteness also leads to conflicting attitudes about the matters on which Joint-councils will have the right to be consulted and information provided hampering their effective functioning. It is, however, clear that with greater experience, and with gradual removal of mutual suspicion, these councils would be playing an increasingly important role in the improvement of industrial relations.

6·2 *Workers' Education.* A scheme has been evolved providing for the training of teacher-administrators and worker-teachers. It is envisaged that the latter, on the completion of their training, will start unit-level classes in their establishments for the rank and file of the workers. The purpose of such education is to raise the self-confidence of the workers and reduce their dependence upon outside leaders. The presence of such trained and educated workers on the Joint Councils should lead to an improvement in the tone of management and ensure the fullest utilisation of protective labour laws passed by the State.

6·3 *The Future.* It is necessary to inculcate amongst workers an urge for material and economic welfare. Planned development involves alround sacrifice and it is necessary that the fruits of progress should be shared in an equitable manner.* The very concept of a socialist society envisages that the economic and social organisation which is being created must assure that individuals and groups are moved more by a desire to maximise the social net product than strive to make private gains at the expense of the general well-being. It has been recognised[63] that:

> "The surpluses that are generated are a social product, to which neither the employer nor the working class can lay an exclusive claim ; their distribution has to be according to the worth of the contribution of each, subject to the requirements of further development and the

*See Vol I Ch. III para 1.

63 Third five year Plan p. 253

> interests of all the sections of society, in particular, the satisfaction of the basic needs of all its members."

Labour must increasingly recognise that neither the policy of its own unions nor that of the Gevernment can be, or should be, directed to providing increasing benefits only to the working class. It is necessary to emphasise that all individuals and groups have a common responsibility and must be moved by 'a sense of mutual obligations than the spirit of acquisitiveness.'

VI

INDUSTRIAL FINANCE

1. Need and Nature of Industrial Finance

1·1 A decade of planning has led to fairly rapid growth of industries and the Third Five Year Plan envisages that the essential foundations for self-sustaining growth would be laid with the completion of the industrial programmes drawn up for the Third Plan. It is estimated that in 1965-66, the general index of industrial production* would reach the level of 329 as against the base of 100 in 1950-51. It is clear that such an enormous expansion of industrial development must require an adequate supply of finance. So far as the requirements of funds for industrial projects in the public sector are concerned, these will obviously be found by Government, though the Third Five Year Plan envisages that about Rs. 300 Crores will be available from the internal resources of public undertakings. It is generally agreed that public enterprises should contribute to the plan resources of the country through its profits and surpluses, but, in view of past experience, doubts have been expressed as to the ability of the public sector in India to provide such surplus to the estimated extent†.

1·2 The financing of the private sector programmes during the third plan period raises greater difficulties. The requirements of finance are for both fixed and working capital and in the past there has undoubtedly been some difficulties in the required funds from coming forward. In the First Five Year Plan an aggregate expenditure on new investments, replacements and modernisation of Rs. 463 crores was envisaged, against which it is estimated that a shortfall of nearly Rs. 225 crores took place. An enquiry into the causes of this shortfall was undertaken by a committee

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* See Vol. I page 232; Ch. VI, of Vol. I provides the background material.

‡ Vide Vol. I pp. 30-40

under the chairmanship of Mr A. D. Shroff, who argued that this was mainly due to the relative decline in prosperity of the classes who were the normal supporters of the capital market. It has sometimes been argued that there are certain factors which adversely affect the willingness to invest in the private sector, *viz.*,

(i) threat of nationalisation,

(ii) unsatisfactory regulation and economic controls,

(iii) excessive burden of direct taxation on particular industries.

(iv) declining profits due to rising labour costs,

(v) procedural uncertainties regarding capital issues, and.

(vi) a preference for debentures and fixed-interest bearing investments following speculative fluctuations in prices of industrial shares.

It is necessary to recognise that a reluctance to invest in equity capital for risky ventures is not, by itself, a proof of an inherent lack of investible funds for expanding private industries. The real difficulty seems to be not so much a lack of capital as its shyness due to the internal weaknesses of the private sector, malpractices and misuses of funds made available through public subscriptions to capital issues and the unsettling effects of violent fluctuations in prices on the stock exchange, some of which at least were manouvered.

1·3 The Third Five Year Plan estimates the sources of supply of funds for industrial and mineral programmes of the private sector as follows :

Source	Amount (Rs. crores)
1, Institutional Agencies	130
2. Direct loans from Government funds	20
3. New issues	200
4. Internal resources (net of repayment liabilities)	600
5. Direct foreign credit participation	300
Total	1250

The total requirements during the period 1961-66 have been estimated to be about Rs. 1350 crores, so that a shortfall of about Rs. 100 Crores is likely[64]. A further difficulty would be the finding of foreign exchange required for achieving the targets of industrial production. The shortage of

64. Third Five Year Plan, p. 464,

foreign exchange is estimated "to amount to not less than Rs. 530 crores"[65] strangely however the Third Five Year Plan makes no specific provision for meeting these shortages, even though it recognises frankly that "Foreign aid or credit to meet these requirements in full is not at present in sight." Thus, instead of a planned measure to deal with an impending shortage of resources, we have only the following vague statement :[66]

> "It cannot be said at this stage in which specific industries the actual performance will fall short of the targets. Much will depend on the success attained in securing foreign collaboration and investment in industries where these are felt to be desirable. An endeavour will, however, be made to ensure the full achievement of targets in the case of industries of high priority."

One can only hope that the optimism underlying the above view would be justified and the country would not have to suffer from an unbalanced plan of investment needs and availability of investment capital. The role of the specialised financial institutions like Industrial Finance Corporations, the National Development Corporation, the Industrial Credit and Investment Corporation and the National Small Industries Corporation will be watched with interest in the context of the admitted shortage of resources for the private sector.

2. Financial Requirements of Industries.

2·1 Industries require capital for two purposes :

(a) Block capital to finance fixed assets. This is required by newly started industries for fixed assets *viz.*,

(i) land
(ii) buildings
(iii) machinery
(iv) appliances of a durable and semi-permanent character.

Established Industries also require capital for block for purposes of extension and replacements.

(b) Working capital to facilitate the running of the business and enabling the conversion of inputs to the outputs. This is required for :

(i) purchase and working up of raw materials,

65. Ibid Chapter XXVI, para 35.
66. Ibid p. 465.

(ii) stocks and stores,

(iii) marketing of products,

(iv) financing outstandings for goods supplied,

(v) day to day expenses of running the factory,

It is necessary to bear in mind that though both block capital and working capital are equally important in the production process, there is an important economic distinction between the two *viz.*, that the former is invested in fixed assets and is held in the nature of more or less permanent investment, while the latter is partly of the nature of permanent or longterm capital and partly of short term finance. The distinction, however, is rather artificial for even the stock of raw materials and manufactured or semi-manufactured goods for a well-established running business can never fall below a certain minimum so that some capital must be permanently required for such purposes and is of the nature of a permanent capital. Strictly speaking, therefore, only that portion of the working capital which is in excess of this minimum is of the nature of true short-term finance.

2·2 It is often held that block capital should generally be supplied by the public and should be obtained through subscriptions by floating in the open market shares or debentures of the industry. In other words, the function of the banking system should be merely to make available funds for floating assets on the basis of the security of stocks and other transferable liquid assets. Theoretically such a distinction would be legitimate only if credit supply by commercial banks only were under consideration, for there is no reason why specialised institutions set up specifically to deal with the supply of industrial finance should not supply both block capital and working capital. Further, such a distinction for demarcating sources of supply of capital would be highly discriminatory for the relative proportions between block and working capital required in an industry varies with the nature of the industry, and the former is apt to bear a larger proportion of the total requirement the more "roundabout" *i.e.* capital-intensive the process. It is a mistaken conservative view to hold that initial block capital for industrial enterprises should be put up by private or public subscription. It is certainly desirable that industrial enterprises should maintain a safe and proper relation between owned capital and borrowed capital, but to envisage that all block capital and even the minimum permanent working capital should be provided by each industrial enterprise out of its own initial capital is to cripple from the start the prospects of industrialization in the country.

3. Shortcomings of Finance for Industries.

3·1 Supply of finance for industries in India has never been properly satisfactory because of the proverbial shyness of Indian capital. The individual investor in India, perhaps because of the *per capita* low rate* of savings, is generally unwilling to take risks by subscribing to issues of industrial share capital nor is direct buying of debentures through the stock exchange particularly popular. In recent times some improvement has been noticeable, though even now the extent of direct subscription to capital issues of industrial enterprises is far from satisfactory. There are reasons to believe that the so called "over-subscriptions" of capital-issues is often illusory and is the result of book transfers through conversion of one form of investment by another so that very little of new net capital formation has been taking place in the form of a larger proportion of the national income coming to be saved and invested. This is, of course, not surprising in view of rise of cost of living often outstripping growth of individual earnings thereby reducing ability to save, while willingness to save must necessarily be low in a period of rising prices (which reduces over time real value of money savings) and an increasing demand for a higher standard of living.

3·2 The main financial handicaps of Indian industries may be summarised as follows :—

(i) Banks in India are reluctant to provide finance for block capital for industries,

(ii) there is little underwriting of industrial capital or even lending money on the security of industrial shares,

(iii) insistence generally on a full backing ef tangible and easily realisable security for loans granted,

(iv) a large margin in regard to advances against stocks, with an even larger margin in regard to stocks in process of manufacture,

(v) non-acceptance of block capital as general security for loans,

(vi) burdensome rates of interest and insufficient length of time for the loans.

3·3 Prior to the inauguration of the era of planning, it might have been possible for the government to adopt a *laissez-faire* attitude towards industrial finance, though even in England, the home of the doctrine of economic neutrality,

* See Vol. I, p. 489-90.

the need for active participation by the Government in the promotion of industrial interests has been steadily recognised even without any overall planning as in India. With the emergence of a planned economy aiming at rapid industrialisation, the old attitude of leaving the supply of capital to the market could hardly be continued, especially when planned development required control over Capital Issues. Further, a national government in charge of the welfare and economic prosperity of an independent country could hardly continue the pre-1947 policy which bred an economic dependence on foreign capital and foreign manufactures. It was necessary to establish specialised institutions—often State-sponsored and aided by the Government—to deal with the needs of the large volume of industrial finance required for planned industrialization of the country. The setting up of special institutions specifically intended to assist and finance the private sector has undoubtedly helped to extend the capital market in India, and, to-day, at least adequacy of industrial finance for private enterprise in India has been provided for, even though the nature of the finance made available may be open to criticism from various points of view. However, some idea of the extent of finance required may be got from the consents granted for issues of capital indicated below :

Year	No. of Consents granted	Amount consented to (Rs Crores) Agriculture and allied activities	Industrial	Non-Industrial	Total
(1)	(2)	(3)	(4)	(5)	(6)
1951	343	—	44·0	15·6	59·6
1955	289	3·2	97·5	24·7	125·4
1956	297	1·8	192·6	35·8	230·2
1957	345	2·4	113·4	37·5	153·3
1958	282	2·8	401·0	19·2	423·0
1959	264	1·3	174·3	27·9	203·5
1960	314	0·9	263·1	25·6	289·6

Source : Controller of Capital Issues.

The trends revealed by the above table are interesting. It appears that non-industrial issues have remained fairly constant during the Second Plan period, but industrial issues have risen steadily, though the peak reached in 1958 has not been subsequently repeated.

4. Some Specialised Agencies for Industrial Finance and Industrial Development.

4. 1 *The Industrial Finance Corporation of India.* This was set up by an Act of Parliament and was established on

July, 1, 1948. It is a shareholders corporation with an authorised capital of Rs. 10 Crores, and has at present an issued and paid up capital of Rs. 5 Crores. The capital has been subscribed by the Central Government, the Reserve Bank of India and institutional investors like the scheduled banks, insurance companies, the Life Insurance Corporation of India, cooperative banks and investment trusts. The Central government has guaranteed the repayment of capital and also a minimum dividend of 2½ percent on the investment.

4·1·1 *Resources.* The Corporation can augment these by the issue of bond and debentures which are guaranteed by the Central Government both in respect of payment of interest and repayment of the principal. It can accept deposits from the public but only for a minimum period of five years so that it does not get restricted in its operation by having to use short-term funds for long-term investments. It can also, under the 1953 amendment, take loans from outside agencies under government guarantee.

4·1·2 *Functions.* The I. F. C. is a very specialised institution intended to promote and assist industrial development in the country. Its role should be that of making possible the establishment and expansion of enterprises that will be of benefit to the public, and to the productive power of the country and provide employment for its people. In short, public advantage rather than profitability to the promoters should be the guiding consideration. The following functions have been entrusted to the corporation :

(a) granting of loans and advances to industrial concerns,

(b) guaranteeing loans raised by industrial concerns,

(c) underwriting the issue of stocks, shares, bonds or debentures by industrial concerns, and,

(d) subscribe directly to the stock or shares of industrial concerns.

The functions under (a) and (b) are restricted, *i.e.*, the former must be repayable within 25 years while the latter can be extended only to those repayable within a period of 25 years and which have been floated in the open market. As regards (c) the provision is that such stocks and shares etc. must be disposed of by the corporation, unless special permission of Government is obtained, within a period of 7 years from acquisition; but, with the authorisation of (d) through the Industrial Finance Corporation (Amendment) Act of 1960, the significance of underwriting and its limitation has ceased to be of importance. It is doubtful whether

the extension of the function under (d) has been either logical or economically desirable. It seems paradoxical to permit a financing agency to provide "equity capital," for the purpose could be served equally well by underwriting under (c) or by purchasing such stocks and shares as investment directly from the open market. It is felt that direct subscription may take the place of loans, and, there would be little protection against bolstering up an issue which would have found no response from the public. In fact, there is no reason why with the underwriting clause alone enough public confidence cannot be brought about so as to eliminate the need altogether for direct subscription. It might indeed be argued that if an enterprise does really need direct subscription to its share capital because it cannot float them in the open market even with underwriting by the corporation, there is something fundamentally wrong with it and the I. F. C. would be well advised to stay away from it.

4·1·3 *Scope.* The I. F. C. can grant loans only to Public Limited Companies and is debarred from assisting Private Limited Companies, Partnerships and industrial concerns owned by the state. This is a wise limitation for an organisation aided and sponsored by the government should be available only for public benefit and not be used for assistance to sectional interests. The exclusion of state-owned enterprises from the scope of the activities of the I. F. C. is only realistic for such enterprises, with the resources of the state itself at its disposal, would hardly require assistance from the I. F. C. It has also been provided that the corporation can grant loans only for long periods; however, since earlier repayment is not debarred, the period of the loan, in effect, has only a maximum duration and not a minimum duration. As a matter of policy, the corporation attaches special importance to the financial needs of large scale industries which are of strategic and national importance. The original Act limited the maximum advance to any individual borrower to Rs. 50 Lakhs, but this was raised in 1953 to Rs. 1 crore, and, by the same amendment shipping companies were included in the definition of industrial concerns eligible for assistance from the corporation. An important feature of the I. F. C. is that it is empowered to make loans either in Indian currency or in any appropriate foreign currency. Such a provision was obviously necessary because much of the industrial development in an under-developed economy requires purchases of plant and equipment from abroad for which provision of loans and assistance with foreign exchange facilities may be very necessary. Further, the I. F. C. is

obviously in a better position to raise loans abroad and logically, therefore, it is in a better position to grant advances in terms of foreign currency in appropriate cases.

4·1·4 *Working.* Initially the corporation had a non-official industrialist as part-time chairman who was obviously unable to devote as much attention to the work of the corporation as was necessary or desirable. Further, it was wrong in principle to entrust the chairmanship to anybody connected with industry itself for the industrial enterprises constituted the chief beneficiaries from the I. F. C. It is unfortunate that within a short-period of four years, Government were compelled to appoint, as a result of considerable public criticism, an Enquiry Committee to examine charges of favouritism and partiality. The Committee, which was under the chairmanship of Mrs. Sucheta Kripalani, submitted its report in May 1953 recommending the appointment of a paid full time chairman. The Enquiry Committee exonerated the management of the Corporation from charges of favouritism but at the same time came to the conclusion that in some cases the advances were unhappy and could have been easily avoided. The main recommendations of of the Committee were :

(i) broad-basing the Board by including a larger variety of experience,

(ii) setting up of regional panel of advisers in every branch office,

(iii) more stringent scrutiny in the case of loans to concerns in which members of the Board were interested,

(iv) reference to Central Government for sanction of all loans in excess of Rs. 50 Lakhs,

(v) maintenance of a minimum margin of 50 percent for all loans with proper assessment of earning capacity of the borrowing concern, and

(vi) publication of detailed information and annual reports.

On the basis of these recommendations, government issued necessary instructions making it obligatory for the Directors to disclose whatever interest they may have in any loan application. The government further instructed the Corporation to keep a minimum margin of 50 percent when sanctioning loans and to obtain prior approval of government whenever a loan meant for an individual firm exceeded Rs. 50 Lakhs.

The I.F.C. has undoubtedly grown in strength with the passage of years and has extended its activities both quantitatively and over a wider field. The table given below illustrates tbe development of the Corporation :

(In Rs. Lakhs)

Year	Liabilities (A)				A or B	Assets (B)		
	Reserves	Bonds and Debentures	Borrowings	Other	Total	Cash & Bank balances	Loans & Advances	Other
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
1951-52	2	5,81	—	5,40	11,23	55	6,55	54
1952-53	3	5,81	—	5,61	11,44	26	8,62	56
1953-54	28	7,81	30	5,46	13,84	5	11,20	59
1954-55	30	7,81	—	5,52	13,62	23	12,78	60
1955-56	49	7,81	61	5,80	14,70	2	14,01	6
1956-57	87	7,81	7,07	6,02	21,75	9	20,70	96
1957-58	60	12,37	15,00	6,09	33,99	5,99	26,20	1,80
1958-59	84	16,75	10,94	6,51	35,04	72	32,10	2,23
1959-60	1,17	22,24	9,13	8,53	41,07	4	36,73	4,30

N.B—Figures as on last Friday Source: Reserve Pank of India.

The steady progress of the Corporation's activities, especially the growth of its reserves is a healthy sign and an indicator of the significant role it has been playing in bringing about the industrial development of India. It is true that the I.F.C so far had to deal only with the easier part of its function *viz.*, granting assistance ; the real test of its efficiency and its having been managed with appropriate prudence will come when the other and more difficult part of its function begins, *viz.*, recovering the loans and advances made earlier.

4·2 *State Financial Corporations.* In a vast country like India, with all its regional differences and the concept of political autonomy for the States, it would be impossible for a single All-India institution to satisfactorily handle the entire problem of industrial finance in a rapidly growing economy. The need for state finance corporations were all the more great because the Industrial Finance Corporation is unable to cater to the financial needs of small and medium-sized industries which are generally private limited companies. Planning in India has recognised that Small-scale

Industries* has a distinct and important role to play in our country. Even the Constitution of India lays down (vide Article 43) that "The State shall endeavour to promote cottage industries...". It has been generally recognised that inadequate finance constitutes the most significant drawback for most small-scale industries. It is difficult for such industries to obtain capital through floating public shares, nor is it generally possible for them to get adequate advances from organised banking. Lack of finance often forces such units to uneconomic borrowing at high rates of interest from private moneylenders with disastrous consequences. These financial difficulties of small and medium-sized industries led the Government of India to pass in 1951 the State Financial Corporations Act. Under this Act, State Finance Corporations have been set up in different States, and at present every State has a Corporation.

4·2·1 *Organization.* Under the Act, the maximum authorised capital of a State Corporation can be Rs. 5 crores. It can issue bonds and debentures upto a limit of five times the amount of its paid-up share capital and reserve fund. In the case of State Corporations, the general public can subscribe to its share capital upto a maximum of 25 per cent of the total.

4·2·2 *Relation with the Reserve Bank of India.* The promotion af these State Finance Corporations has been an important responsibility of the Reserve Bank and it has collaborated with them through being an important shareholder in each case. The Reserve Bank not only has the power to inspect these corporations but also functions as the coordinating agency between these Corporations and the rest of the banking system including the State Bank of India and the Cooperative Banks. As between the Industrial Finance Corporations and the State Corporations, a working arrangement for coordination has been evolved through the adoption of the convention that while the latter will confine itself only to loans upto a maximum of Rs. 10 Lakhs, the former should entertain loans for amouts in excess of Rs. 10 Lakhs.

4·2·3 *Scope and Functions.* The State Corporations can grant loans to private limited companies, partnerships and even proprietory concerns. Thus, while the I.F.C. is limited in its operation only to public limited companies, the State Corporations are not so limited. But on the other hand, the State Corporations can give guarantee and make advances for a maximum period of 20 years as against the 25 years

*See Vol. I pp. 246-251.

for which the I.F.C. can extend its help. The State Corporations generally confine themselves to loan capital used by the borrowing units for periodical expansion and replacement The S.F.Cs. have generally avoided providing 'equity capital for initial investment and have not also extended much help towards providing working capital for day-to-day operations. This is because the S.F.Cs are more or less limited to mortgage financing technique and have refrained from taking what may be called legitimate risks for promoting development. This also explains why the State Corporations have provided more financial assistance to medium-sized concerns than small units, for the latter are usually more 'risky' borrowers often lacking in sufficient pledgable fixed assets.

4·2·4 *Working and Achievment*—It was not till 1961 that all the 15 States in India were able to set up State Finance Corporations. It is, therefore, difficult to assess with any degree of accuracy their comparative progress since some of them have been in the field much longer than others, However, some idea of the comparative State-wise picture is indicated in the table given below :

TABLE for para 4·2·4 State Financial Corporations

(In lakhs of rupees)

	Liabilities					Assets			
	Number of Corporations	Capital and Reserves	Bonds and debentures	Other liabilities	Total liabilities or Assets	Cash in hand & balances with banks	Investment in Govt. Securities	Loans and Advances	Other Assets Include Debentures
(1)*	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
1955	7	5,98	—	1,12	7,10	3,23	2,67	1,06	14
1956	12	10,29	—	40	10,70	3,60	3,94	2,72	44
1957	11	12,36	36	2,03	14,75	3,59	4,01	6,50	65
1958	12	13,21	2,60	2,23	18,04	4,60	3,06	9,35	1,03
1959	12	13,46	6,12	3,74	23,32	7,92	2,80	11,34	1,26
1960	13	14,48	7,17	4,73	26,38	7,21	3,22	13,90	2,05
1961	15	15,43	7,17	7,20	29,80	4,56	4,60	17,12	3,52

* Last Friday Figures.

State Financial Corporations
1961

(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Andhra Pradesh	1	1,52	—	22	1,74	48	31	68	27
Assam	1	1,01	55	48	2,04	84	—	1,03	11
Bihar	1	1,00	1,00	14	2,14	1,67	—	1,32	16
Bombay	1	2,04	1,14	11	3,28	1,07	65	1,42	14
Kerala	1	1,01	55	11	1,67	26	7	1,25	8
Madhya Pradesh	1	1,01	—	10	1,11	31	22	50	9
Madras	1	1,36	1,36	2,90	5,62	72	63	3,65	62
Mysore	1	1,00	—	3	1,03	82	15	4	1
Orissa	1	50	—	5	55	32	9	13	1
Punjab	1	1,01	1,03	19	2,22	44	38	1,20	20
Rajasthan	1	1,00	—	14	1,14	16	45	43	10
Uttar Pradesh	1	1,00	55	11	1,66	49	26	80	12
West Bengal	1	1,01	1,00	18	2,19	64	—	1,39	16

The steady growth in the figure of loans and advances shows that the S. F. Cs have been playing an increasingly significant role during the last few years. It is to be noted, however, that there is a general complaint that the cost of borrowing from the State Corporations is fairly high. This is mainly because of the guaranteed dividend rate to its shareholders which has been fixed at 3½ percent so that the lending rate is rarely below 6 or 7 percent. Further, the borrowing concern has generally to also bear the charges for registration and stamp duty which adds upto another 3 percent, making the total cost of borrowing fairly high and often bordering on an uneconomic rate. However, in spite of this the total borrowings from the S. F. Cs have been increasing from year to year indicating perhaps the high profitability of the borrowing enterprises. This is not unnatural in an expansionist economy with a rising level of prices ; but such a development can hardly be expected to lay the foundations of a truly stable development for small and medium industries. Finally, the S. F. Cs are essentially financing institutions and the true test of the wisdom of their investment policy would come when repayments begin to acquire significant proportions.

4·3 *National Industrial Development Corporation.* This was set up in October 1954. Its capital was provided entirely by the Central Government. It is expected to finance industries required for planned development and to start new

industries where private enterprise is reluctant to initiate investment. The N. I. D. C. has, in addition, two rather specialized functions, *viz*,.

(a) managing temporarily industrial units till they are fit to be transferred to private management, and

(b) granting special loans for rationalisation and modernisation of the cotton textile and jute industries.

Unfortunately, the functioning of the N. I. D. C. has been so far of rather a routine type. Even though all the finances required by it are being provided by the Government of India, it continues to refrain from initiating development either in the relatively backward areas or to sponsor new and unusual, but socially useful, enterprises. It appears that due to unimaginative investment policy, it is becoming another routine loan-giving agency rather than play its appropriate role of giving a lead to private enterprise to promote balanced industrial development in various regions and give a social bias to economic enterprise. On the whole the financial operations of the corporation have been not as imaginative as one would expect it to have in view of its specialized functions. The table given below throws interesting light :

Operations in the year 1959-60.

Financial :

Profit and Loss Account for the Period 1st January 1959 to 31st March, 1960

	(Rs.)		(Rs.)
Expenditure on projects	14,58,404	Interest on loans to industry	21,43,651
Salaries and allowances	2,48,525	Interest on securities	11,606
Expenditure on working group of cotton textile industry	52,407	Miscellaneous income	1,18,797
		Leave salary, pension contributions recovered and miscellaneous adjustments	1,88,584
Interest on loans	21,46,931	Balance being grant due from Govt. of India towards :	
Other items of expenditure	1,45,798	(*a*) projects	12,85,192
		(*b*) other expenditure	3,04,235
Total	40,52,065	Total	40,52,065

Source—C.S.O.

On the projects side, the corporation has undertaken various studies which have led to certain schemes of development being assigned to the private sector while a few, mainly of a pilot nature, have been taken up in the public sector with foreign collaboration. In order to promote the establishment of design and consultation services in the country, a Technological Consultancy Bureau has been set up by the corporation. It is proposed that the Bureau will undertake preliminary studies to help in establishing a project and will also provide subsequent design and consultancy service.

4·4 *Industrial Credit and Investment Corporation of India.* This was set up in January, 1955 as a result of the recommendation of a mission providing discussion between the World Bank, the U.S. Government and the Government of India. The idea was to set up a sponsored private limited company to encourage the growth of private industry. In a sense, it is a characteristic feature of India's faith in the concept of a mixed economy where planned assistance to ensure the continued profitability of privately-owned economic enterprises in a socialistic pattern of economic life is neither a paradox nor a misnomer.

4·4·1 The corporation has an authorised capital of Rs. 25 crores though its paid up capital is only Rs. 5 crores. The paid up capital has been subscribed wholly by private investors both foreign and domestic. The shares of the corporation have been subscribed by British and American Investors, institutional investors, by banks and insurance companies in India and by private individuals.

4·4·2 The Corporation obtained additional resources in the following ways :—

(1) An interest-free loan of Rs. 3·5 crores from the Government of India, repayable in 15 instalments, the first instalment of repayment being due after the expiry of 15 years ;

(2) A 10 million U. S. dollars (*i.e.* about Rs. 5 crores) initially made available in foreign currency by the World Bank on the guarantee of the Government of India ; this has been increased from time to time making a total of $40 millions ;

(3) An interest-free deposit of Rs. 7·5 crores from the U.S. Technical Co-operation Administration ;

(4) A loan of $5 millions (about Rs. 2 38 crores) approved by the Development Loan Fund.

4·4·3 *Functions.* The Corporation is primarily concerned with the development of industries in the private

sector. It aims at expanding the private sector and promote its development by extending assistance to a large number of companies in small amounts, rather than providing large-scale aid to a small number. It performs its functions by :

(a) granting loans and advances to assist in expansion and modernisation,

(b) promoting new concerns by
 (i) providing a part of the 'equity capital',
 (ii) undertaking underwriting operations,

(c) providing managerial, technical and administrative advice and assisting industries in obtaining such advice, and

(d) making available, during an acute scarcity of foreign exchange, assistance in foreign currency for industry in the private sector.

4·4·4 *Activities.* In the course of six years, the Corporation has considerably extended its activities, and has, upto 1960, sanctioned financial assistance amounting to nearly Rs. 32 crores to about 100 Companies. The real merit of its activities has been its attempt to refrain from functioning as an unimaginative lending organisation. It has not confined itself merely to giving of advances against assured collateral security, but it has genuinely financed and promoted industrial growth by investing in share capital and through underwriting of shares. However, the crucial test would be its ability to sponsor private enterprise in a manner consistent with the planning policy of the country which lays down[67] that "within the field of activity entrusted to the private sector, the major aim of policy is to ensure broad-based ownership in industry, diffusion of enterprise and liberal facilities for new entrants, and the growth of co-operative organisations."

4·5 *National Small Industries Corporation.* This was set up in February, 1955 and was registered as a limited company. It has four subsidiary corporations, also registered as limited companies, at Bombay, Calcutta, Delhi and Madras. The authorised capital of the corporation has been provided entirely by the Government of India. The affairs of the corporation are managed by a Board of Directors consisting of 11 members, comprising both officials and non-officials. The capital structure of the corporation is indicated in the table given on the next page.

67. Third Five Year Plan, Ch. I, para 28.

TABLE for 4·5

Balance Sheet as on 31st March, 1960

As at 31-3-1959	Liabilities	As at 31-3-1960	As at 31-3-1959	Assets	As at 31-3-1960
(Rs.)		(Rs.)	(Rs.)		(Rs.)
40,00,000	Issued, subscribed & paid up capital	40,00;000	62,53,575	Fixed assets	1,17,68,629
19,40,102	Reserve & surplus	76,12,989	10,00,000	Investments (at cost)	10,02,675
			57,60,064	Current assets	43,17,061
2,70,64,583	Unsecured loans from Govt. of India.	3,60,37,981	1,92,40,553	Loans and advances	3,24,67,195
			1,66,923	Security & Other deposits	1,07,538
48,60,104	Current liabilities & provisions	52,30,510			
..	Suspense account	12,560	54,39,589	Cash and bank balances	32,23,724
			4,015	Miscellaneous expenses & losses	7,218
3,78,64,789	Total	5,28,94,040	3,78,64,789	Total	5,28,94,040

Source : C.S.O

4·5·1 *Functions.* The activities of the corporation fall under two groups, *viz*,. (a) commercial, (b) promotional.

The former are financed out of loans given by the Government of India since the share capital of the corporation is low compared to the magnitude of the schemes to be undertaken. So far as (b) is concerned, these are financed out of grants made available by the Government of India as these promotional activities involve implementation of schemes which are not revenue-yielding. The functions of the corporation may be briefly summed up as follows :

(i) assistance to small scale units to enable them to participate in store-purchase programmes of the government,

(ii) facilities for marketing at home and abroad,

(iii) arrangements for import of components and their distribution to approved small scale assemblers,

(iv) making arrangements to supply machines on hire purchase,

(v) construction and management of industrial estates,

(vi) establishment and running of Production-*cum*-Training Centres.

In a developing economy, the competitive position of small scale units is generally weak and the need for special assistance* for enabling their continued existence is often a matter of considerable controversy. It has, however, been recognised that to make small scale units economically viable, it is necessary to achieve for them a balanced industrial structure through development of ancillary industrial units. The Corporation has been attempting to achieve this through a twin policy of encouraging large units to purchase their requirements from small units, and, developing a colony of small units in the vicinity of a large unit so that the former can be a feeder to the latter. In this policy the corporation is being assisted by the Small-Scale Industries Service Institutes. Further, no long-period economic advantage can be secured for small-scale units unless fresh technical skill and uptodate machinery are made available. The Corporation has made arrangements for making available such assistance to existing as well as newly established units. Finally, the financial requirements of small-scale units are specially being attended to, and, the corporation is empowered to underwrite and guarantee loans from banks and similar institutions to small units. However, the assistance of the corporation can be availed of only by units with a capital investment of less than Rs. 5 lakhs and employing less than 100 persons when working without power or less than 50 persons when using power.

4·5·2 *Review of Work Done.* The corporation has rightly concentrated on making available assistance for obtaining machinery and machine tools to small scale enterprises at particularly liberal terms so as to enable a larger number of units to avail of these benefits. Generally such assistance is made available through the hire-purchase system. It also pursues a policy of preferentially lower terms to industrial co-operatives both because of the declared plan objective of encouraging their development as also because of their higher creditworthyness. The more important and useful part of the corporation's work has been, however, in the realm of marketing and improving the quality, with standardisation, of the products of small scale units. The Corporation has instituted a system of inspection and is attempting to ensure the production of goods of standardised quality. The working of the corporation revealed,[68] in 1958-59, a loss (total) of Rs. 3,78,56, with a government subsidy of Rs. 34,22. The financial operations in 1959-60 are indicated in the table given on next page.

*See Vol. I, Ch. VI para 8.

68. C.S.O.—Principal Public Sector Undertakings, Section IV, Summary table 3.

TABLE for 4·5·2

Operations in 1959-60.

Financial:

As at 31st March, 1960.		Rs. in lakhs.
Share capital wholly provided by Govt. of India . . .		40.00
Loans received from Govt. of India		360.38
Grant receivable from Govt. of India during the year :	(Rs. in lakhs)	
Expenditure incurred on promotional activities . .	35.90	
Less Grant received during the year including carry overs and adjustments	33.18	
Balance receivable	2,72	
Less net profit earned by the Corporation on commercial activities set off against the above.	1.09	
Net balance adjustable	1·63	

Source—C.S.O.

4·6 *Indian Handicrafts Development Corporation.* This was set up in April, 1958 as a private limited company under the Companies Act, 1956. Its Capital Structure is as follows :

Balance Sheet as at 31st March, 1960

As at 31-3-59	Liabilities	As at 31-3-60	As at 31-3-59	Assets	As at 31-3-60
(Rs.)		(Rs.)	(Rs.)		(Rs.)
10,00,000	Subscribed and paid up capital . .	10,00,000	42,454	Gross fixed assets .	47,785
1,33,911	Current liabilities and provisions . .	46,151	1,483	Depreciation . . .	7,333
			40,971	Net fixed assets . .	40,452
—	Grant appropriation account (Balance of grant held)	59,075	39,767	Current assets . .	45,659
			1,19.666	Loans and advances .	1,55,404
			9,17,088	Cash and bank. balances	. 8,59,116
			16,419	Miscellaneous expenses	. 4,595
11,33,911	TOTAL	11,05,226	11,33,911	TOTAL	11.05,226

Source : C.S O

It has been established mainly to undertake export of handicrafts, khadi and products of village industries and to create favourable conditions for increasing the export of handicrafts. The corporation however extends its assistance

also to giving technical, financial and other assistance including supply of raw-materials, tools, equipment, etc. to exporters and producers.

4·6·1 *Functions*. The corporation performs a variety of functions covering export promotion, marketing and sales, improvement in design and finance. Its main activities may be grouped as follows :

(a) *Financial assistance* by providing short-term credit to exporters to execute firm export orders.

(b) *Raw materials assistance* through making available raw material of appropriate quality at reasonable prices as a high standard of production can be ensured only if proper raw-material supply can be arranged. The corporation arranges to import copper, zinc, polishing material and packing tissue-paper. The imported material is made available to producers under an Export Promotion Incentive Scheme.

(c) *Publicity assistance* by taking part in exhibitions and fairs and booking bulk orders through such displays. The corporation has arranged a network of sales agencies abroad and has established some permanent show-rooms in a few big foreign cities.

(d) *Market in'elligence* by giving information relating to commercial practices, tastes and demand peculiarities, production techniques etc.

(e) *Design assistance* through expert and specialised advice and help on suitable designing of decorative products.

(f) *Quality control* by endeavouring to ensure that orders placed with its business associates are executed in conformity with specification and making certain that there is uniformity in the quality of goods supplied. To assist in this process it has instituted a pre-shipment inspection scheme on a voluntary basis.

4·6. 2. *Review of Achievement*. Whatever benefit the corporation may have brough to the small scale industries, its financial working has so far led to substantial losses which were Rs. 12,651 in 1958-59 and Rs. 2,53,274 in 1959-60. The table on next page indicates its financial operations.

(i) Income and Expenditure Account
for the year ended 31-3-60

As at 31-3-59	Expenditure	As at 31-3-60	As at 31-3-59	Income	As at 31-3-60
(Rs.)		(Rs.)	(Rs.)		(Rs.)
			2,374	Income on foreign consignment and samples	536
96,200	Salaries and allowances	1,48,592			
2,00,616	Trade development expenses	72,489	1,530	Interest on loans	9,002
				Interest on short-term deposit account	7,748
1,483	Depreciation	5,851			
38,256	Other expenses	45,442		Other income items	1,824
			3,32,651	Deficit carried to Grant appropriation Account	2,53,274
3,36,555	Total	2,72,374	3,36,555	Total	2,72,374

(ii) Grant Appropriation Account

	30-3-60		
	(Rs.)		(Rs.)
Deficit 1958-59 brought forward	12,651	Grant received from Government	3,25,000
Deficit for the year brought down from Income Expenditure account	2,53,274		
Balance carried over to balance sheet	59,075		
Total	3,25,000	Total	3,25,000

Source : C. S. O.

It will be seen that but for the enormous subsidy received from government, it would have been impossible for the corporation to carry on its activities. It is a matter

for consideration* whether revival of small scale and cottage industries by transfer of resources through the medium of government subsidies increases net economic welfare for the country or not.

4·7 *Refinance Corporation for Industry.* This was established in June, 1958 and is a registered private limited company under the Companies Act, 1956. The main object of the corporation is channelling and disbursing the American counterpart funds of the Agricultural Commodities Agreement under what is commonly known as P.L. 480‡. The corporation would make aid available, on a medium term basis, to those industries which are listed for development in the private sector under the Plan. The re-lending operations of the amount (about Rs. 26 crores) constitutes the basic function of the corporation; though its resources have been augmented by other sources. The capital structure of the corporation is indicated below :

Capital Structure.

Balance Sheet as at 31-12-1959

As at 31-12-1958	Liabilities	As at 31-12-1959	As at 31-12-58	Assets	As at 31-12-59
(Rs.)		(Rs.)	(Rs.)		(Rs.)
2,50,00,000	Subscribed and paid up capital.	2,50,00,000	3,545	Fixed assets . .	,332
			99	Library books.	85,00,000
			. .	Loans to member banks	
8,393	Reserves and surplus.	1,09,331		Interest accrued :	
5,00,00,000	Unsecured loan from Government of India.	5,00,00,000	3,79,555	On short term deposits	2,90,323
			...	On loan to member banks	85,548
45,002	Sundry creditors.	71,041	...	Advance payment of taxes	13,60,344
2,31,507	Interest accrued on loan from Government of India.	8,75,000	7,59,48,457	Cash and bank balance	6,82,97,825
5,81,000	Provision for taxation.	14,82,000			
4,65,754	Proposed dividends.	10,00,000			
7,63,61656	Total	7.85,37,372	7,63,31,656	Total	7,85,37,372

Source : C. S. O.

4·7.1 *Aim and Functions.* The corporation aims at encouraging commercial banks to expand medium term finance

* See Vol. I. pp. 247-248.

‡ See Vol. I, p 492.

for industry by providing re-finance facilities. During 1959, the corporation provided Rs. 225 lakhs, bringing the total re-finance sanctioned since its inception to Rs. 403 Lakhs. The facilities are generally intended to be confined to medium sized units for :

(i) an individual loan does not normally exceed Rs. 50 lakhs,

(ii) loans are to be made available only to units whose paid up capital and reserves are not less than Rs. 5 lakhs but not more than Rs. 2·5 crores,

(iii) the period of the loans is between 3 and 7 years.

4 7·2 *Operations.* The corporation has adopted rather a cautious attitude and the demands on it have not been able to use up its funds fast enough. It is true that other alternative sources of finance together with the growing volume of bank deposits have reduced the need for re-finance activities ; but, even then it would appear that the achievements of the corporation have hardly justified the setting up of a special institution to handle the P.L. 480 counterpart funds which could equally easily, and with perhaps greater efficiency, be made available to the Industrial Finance Corporation. The limited nature of its activities would be illustrated from the details of its financial operations given below :

(i) Profit and Loss Account for the year ended 31st December, 1959

For the period from 5-6-1958 to 31-12-1958		For the year ended 31-12-59	For the period from 5-6-1958 to 31-12-58		For the year ended 31-12-59
(Rs.)		(Rs.)	(Rs.)		(Rs.)
41,752	Amount paid to the Reserve Bank of India in respect of establishment and other charges	70,041	14,09,304	Interest on monies placed on call & short term deposits with banks	27,51,340
2,31,507	Interest on loan from Government of India.	8,75,000	..	Interest on loans to member banks.	2,05,548
9,171	Other expenses	9,910	7	Miscellaneous reciepts	1
11,26,881	Balance, being profit subject to taxation, carried forward	20,01,938			
14,09,311	Total	29,56,889	14,09,311	Total	29,56,889

(ii) Appropriation Account

Rs.		Rs.	Rs.		Rs.
5,81,000	Provision for taxation	9,01,000	..	Balance brought forward	8,93
71,735	Preliminary expenses written off.		11,26,881	Balance being profit subject to taxation	20,01,938
..	Transferred to General Reserve	1,00,000			
4,65,753	Proposed dividend at the rate of 4% p. a. subject to tax	10,00,000			
8,393	Balance carried forward	9,331			
11,26,881	Total	20,10,331	11,26,881	Total	20,10,331

Source : C. S. O.

The need for greater flexibility in its operations has been recognised and the corporation has to extend its activities even to other banks who are not shareholders. Further, there seems little necessity of insisting on a minimum spread between the rate at which the member banks borrow from the corporation and the rate at which they lend to industrial units, for all that is necessary to prevent misuse is to ensure that the final lending rates are not too high and are subject to review by the corporation.

5. The Managing Agency System of Finance.

5·1 *Characteristic Features of Managing Agency System.* The Managing Agency system is a special, and in a sense a unique, feature of Indian industrial organisation. It has, of late, come in for so much criticism that one is perhaps apt to forget that, though not without demerits, it has played an important role in the industrial development of India. A managing agency firm is generally a partnership firm or a private limited company, though of late there has been a trend towards conversion into limited liability companies. These firms are an important link in the industrial system performing the following functions :

(i) promoting new business by floating shares of new concerns and holding them temporarily,

(ii) supplying regularly trained personnel capable of discharging the duties of efficient management,

(iii) undertaking management of the companies under their control,

(iv) performing the pioneering work of investigation and research preceding the initiation of a new enterprise,

(v) making available funds and arranging for finance by acting as guarantors.

5·2 *Financial Assistance.* The system has in the past undoubtedly performed a creditable serivce to industries in India by extending considerable financial assistance through,

(a) direct loans,

(b) guarantees for bank advances,

(c) attracting deposits by associating their credit,

(d) subscribing to shares and debentures,

(e) placing the securities of the companies under their control on the market.

To appreciate properly the functions of industrial finance performed by the managing agency system, it is necessary to remember that their most important roles were played at a time whem no specialized agencies had been brought into existence for tackling the financial needs of industries, and when Indian capital, proverbially shy, was most reluctant to come forward to take the risks of industrial development in its early stages. In fact, it is doubtful if the early beginnings of industrial enterprise could have been laid but for the enterprise and initiative of the managing agents, especially as commercial banks in India have invariably been reluctant to extend financial assistance for the development of industries. It is, however, necessary to bear in mind that the managing agency system of finance has not been free from defects and has, in fact, been often abused to the detriment of individual industries and the economy. The most serious defect that followed was the subordination of management to finance and the growth of concentration of economic power* through financial control of a number of companies passing into the hands of a single managing agent. It has often been seen that where one managing agency firm manages a number of industrial concerns, there is a tendency for all of them to react similarly and the distinction between good and bad concerns very often fades into the background. There were many occasions when, through the medium of a common managing agent, transfer of funds from a successful concern to an unsatisfactory one has taken place to the detriment of the interests of the shareholders of the prosperous unit. Finally, there have been serious allegations of speculative activity in the share-market by the managing agents with a view to getting managing control by acquiring predominant holding of shares.

*See Vol. I pp. 239—243.

5·3 Legal Control Over the Managing Agency System.

5·3·1 In spite of the many important contributions made by the managing agents, the system has for a long time been subject to regulation and control. A few important restrictions were imposed in 1936, but these were never seriously enforced. The criticisms against the managing agency system continued and after independence, the government realised the urgent necessity of bringing about a comprehensive reform in it. The Government of India, therefore, appointed in 1950 a Company Law Committee, known as the Bhabha Committee, to review the entire situation. On the basis of the report of this Committee, the 1956 Companies Act provided for important measures of control over the Managing Agency System. The main provisions of the 1956 Act were as follows :—

(i) The Government can, on the advice of a Committee specifically appointed for the purpose, declare that all companies in certain classes of industry or business shall cease to be managed by Managing Agents,

(ii) After the commencement of the Act, approval of the Central Government is necessary for the appointment of Managing Agents, who can now be appointed only for a period of 15 years in the first instance, and renewed for not more than 10 years at a time,

(iii) Restrictions have been imposed on grant of inter-company loans under the same Managing Agency firm as also on the purchase of shares or engagement in competing business of firms under it,

(iv) Limitation of the total number of Companies to a maximum of 10 for purposes of management by a single agency.

5·3·2 The 1956 Companies Act attempted to rigidly control the managing agency system but failed to recognise that as long as the private sector exists, it must earn adequate remuneration. The 1956 Act permitted a maximum remuneration to Managing Agents of upto 10 percent of net porfits. There was, of course, provision to the effect that additional remuneration in excess of the prescribed maximum could be paid by means of a special resolution of the company subject to there being no objection from the Central Government. Unless relaxation to the prescribed maximum remuneration becomes a general rule, rather than remain an

exception as was obviously envisaged, it is doubtful whether the smaller Managing Agents would be able to expand old business or promote new ones. It is possible, therefore, that indirectly it may lead to the very evils of concentrated prosperity and monopolistic growth of economic power which is intended to be combated as an objective in the Third Five Year Plan.

5·3·3 The Company Act was further amended in 1960 on the basis of the recommendations of a Committee appointed by the Government of India under the Chairmanship of Shri A.V. Vishwanath Shastri. The amended provision attempted a stricter definition of "remuneration" of Managing Agents and prohibited any contract for the rendering of any service between a Company and its Managing Agent or any associate of the Managing Agent unless such contract was approved by the company by a special resolution and was also accepted by the Central Government. It has been estimated[69] that the managing agency remuneration as percentage of profits before tax worked out as follows :

1955	...	14·2%
1956	...	11·5%
1957	...	11·7%

The above estimates, however, exclude some of the 'invisible' earnings of managing agents from such sources as sale and purchase of goods and supply of services etc. ; but excluding such items there is a clear indication that the income of the managing agents has been on the decline. It may be noted that the reason why the percentage figures given above are higher than 10% which is the statutory maximum under the Companies Act is simply that some companies, despite a low level of profits (or even losses sustained) paid the minimum managing agency remuneration as given in the managing agency agreements.

5·4 *The Future of Managing Agency System.* It is clear that on an ideological basis, there is no justification for permitting the continued existence of the system. Apart from ideological reasons, it can be argued that even froma purely economic point of view, the system has outlived its necessity and it is now a drag on the economic system rather than an aid to development. It would seem that with the active role played by the State in industrial financing through the various specialized agencies, the managing agency system is no longer the main or even an important source of obtaining finance for industry. Further, the growing significance of the public sector and the increasing emphasis laid on the

69. For details see Reserve Bank of India Bulletin, August, 1959.

public purpose of the private sector, there can be no further necessity or justification for the continued existence of the managing agency system.

6. Foreign Capital and the Financing of Industrial Development.

6·1 It would be useful to draw a distinction between foreign capital and external assistance,* meaning by the former private foreign investments in India and indicating by the latter assistance obtained at governmental level. The distinction, of course, is rather loose for in a planned economy with intensive control on Capital Issues and severe regulation of foreign exchange releases, new private inflow of foreign capital is hardly a large-scale practical feasibility. There are, however, a large number of branches of foreign companies operating in India and foreign controlled rupee companies. There may also be small holdings of shares in Indian rupee companies by foreigners. In their economic effects, there is no fundamental distinction between foreign capital and external assistance for the transfer effects and the effect on balance of payments must be identical for both represent inflows and outflows of funds.

6·2 *Estimates.* The total foreign capital investment in India is difficult to estimate. The Reserve Bank of India has attempted [70] to collect data regarding foreign investments and estimated that the total foreign business investments in India amounted on the 30th June 1948 to Rs. 320·42 crores. According to a later estimate of the Reserve Bank of India, the total foreign investments in the private sector in India amounted to Rs. 508·7 crores at the end of 1957, of which the investments in the foreign controlled enterprises or foreign direct investment amounted to as much as Rs. 446·1 crores *i.e.*, nearly 87%. The comparability of the figures of 1948 and 1957 is, however, limited because the coverage was limited and also because the units included were not identical. In its recent analysis, the Reserve Bank of India[71] points out :—

> "There were in all 565 branches of foreign companies which were registered in India as on 31st March 1960. Nearly two-fifths of these represented branches of financial institutions including banks and insurance companies, non-profit organisations and airlines and shipping companies, and such other branches as have already gone into liquida-

* See Vol. I, Ch. XII.
70 Survey of India's Foreign Liabilities and Assets 1957.
71. Bulletin, March, 1962 p. 344.

> tion or as have ceased to function. The book value of total assets held in India of the remaining three-fifths of the branches amounted to about Rs. 427 crores as at the end of 1959."

The detailed study of 207 branches of foreign companies and 117 foreign-controlled rupee companies shows the following intersting trend :

(In Rs. Lakhs)

	Total Net Assets at the end of 1957	1958	1959	Percentage growth in 1959 over 1957
Branches of Foreign Companies	298,35	294,32	305,86	+ 2·5
Foreign Controlled Rupee Companies	306,24	327,05	348,84	+13·9

6·3 *Economics of Foreign Capital.* Recent thinking on the economics of growth tends to support the view that use of foreign capital in an underdeveloped country is necessary and desirable as it tends to increase not only the rate of development but also stimulates domestic savings. The inauguration of the era of planning in India frankly recognised the inescapable necessity of external finance and observed :—

> "India has a programme of development larger than can be financed from the resources internally available. There will remain certain shortages which would tend to restrain the whole pace of development and it is in meeting these that external resources will be of help."[72]

In short, foreign capital may help to quickly increase the availability of total resources and thereby accelerate the country's economic development. An economy in transition inevitably puts a high burden on the consumer, and, it is not unreasonable to speed up the pace of development with a view to shortening the period of the burden. It is true that if the rate of domestic savings could be enhanced sufficiently so as to provide internally adequate resources for achieving the desired rate of investment and capital formation, the use of foreign capital could be rigidly limited, especially if the

72. First Five Year Plan, p. 27.

cost of borrowing in the foreign market (or, what comes to the same thing, the returns expected by the foreign investor) is high. There are, however, reasons to believe* that the potential rate of domestic saving in India would hardly be able to reach the required level.

6·4 *Causes of Distrust of Foriegn Capital.* The reluctance to use foreign capital is based more on non-economic than economic grounds. The fear that vested foreign interests may grow up or that the foreign capitalist may be more interested in earning a large return in a short period than in laying a true and stable foundation for industrialization are obviously relics of the past. It can be safely believed that the Government of India today are quite competent to prevent any unhealthy activities of the foreign investor. In any case ,a growing tendency is noticeable for the foreign capital to identify itself more and more with the economic interests of India so that the old fear and distrust may now be regarded as a thing of the past.

6·5 *The State and Foreign Capital.* The Industrial Policy Resolution issued in 1948 within a short period after independence contained a definite bias towards nationalisation and also introduced some restrictions on the use of foreign capital. In 1949, however, the Prime Minister made a policy-statement which contained clear and categorical assurances to foreign capital indicating :

(a) non-discrimination as between foreign and Indian undertakings,

(b) provision of facilities, subject to availability of foreign exchange, for remittance of profits and repatriation of cpital, and,

(c) provision of fair compensation in the event of nationalisation, which itself was not regarded as an immediate possibility.

Subsequent Indian policy has shown little change to the disadvantage of foreign capital and facilities have continued to be given for fairly free remittance abroad of profits of foreign business concerns. It must, however, be recognised that while the early disinvestment of private foreign capital that took place in the period immediately following the country's Independence was arrested, the growth of private foreign investment in India has not been as rapid as is sometimes believed. A study of the figures of foreign investment in India would show that the total foreign capital investment in the private sector is indeed not

* See Vol. I, pp. 489—490.

very large, nor is its growth either alarming or excessive. The following table illustrates [73] the position :—

Outstanding Foreign Investment in the Private Sector

(In Rs. Crores)

Year (June)	from private sources abroad	from offical sources abroad	Total
(1)	(2)	(3)	(4)
1948	255·8	——	255·8
1955	453.3	2·7	456·0
1956	478·0	14·8	492·8
1957	494·8	46·9	541·7
1958	498·4	72·2	570·6

N.B. Figures exclude investment in the Banking Industry.

In recent times, there is an obvious tendency noticeable for the inflow of foreign capital on private account to decline in view of the entry into the field of private enterprise financing by such institutions as the World Bank and international financing agencies. The following figures [74] illustrate the trend :

Net Inflow of Foreign Investment into the Private Sector

(In Rs. Croras)

Year	Private foroeign capital	I.B.R.D. capital	Total
(1)	(2)	(3)	(4)
1954—55 (annual average)	14·9	1·4	16·3
1956	24·7	12·1	36·8
1957	16·8	32·1	48·9
1958	1·7	25 3	27·0

6·6 *The Future.* The general tempo of development has shown an alround increase in practically all the under-developed countries of the world. There has been a wide-spread expansion in the scale of business enterprise all the world over. The demand for "risk capital" has steadily

73 Reserve Bank of India Bulletin, April 1960.
74 Reserve Bank of India Bulletin, April 1960.

increased, making the position of countries like India, which are still under-developed but not so under-developed as to require the foreign capitalist along with foreign capital, relatively disadvantageous as regards foreign capital supply. There is, therefore, an inevitable growth of joint association of Indian risk capital with its foreign counterpart. This may not entirely and fully solve the problem of capital supply but would certainly go a long way towards speeding up the industrialization of the country.

VII

TRADE AND TRANSPORT

1. The Background of Indian Economy with reference to Trade.

1·1 1960-61 marked the final year of the Second Five Year Plan and witnessed a striking advance in industrial production, an improvement in agricultural output specially food-grains and a rise in aggregate investment. All this naturally led to a rise in the National Income, which in turn would normally be expected to increase the contribution of trade and commerce to the aggregate income. It is well-known that the volume of transport is normally a reflex of the aggregate volume of trade, though generally the rise in the demand for transport is usually relatively faster than the growth in trade because of changes in the lead of traffic and increases in multiple and cross movements which are in themselves a characteristic feature of an expandiug industrial economy.

1·2 1961-62, the first year of the Third Five Year Plan, achieved further increases in developmental outlays in the public as well as the private sector, and, substantial increases in agricultural and industrial production led to supply conditions being on the whole favourable. In fact, there were obvious signs of a better balance between supply and demand in the economy as a whole. However, the trade and commerce of a country is not merely an aggregate of transactions but significant aspects of it are related to individual sectors, and, it is not unusual to have a large measure of stability in the economy with signs of weakness or imbalance in individual sectors. It may, therefore, be noted that there were situations of scarcity from time to time in some important sectors, including, in particular, power, transport, coal and some varieties of steel. Among agricultural commodities, supplies of raw jute and oilseeds showed unsatisfactory trends during the early months of 1961.

1·3 The index of industrial production* is usually the best indicator of the growth of trade in India, as practically the whole of it enters the monetised sector of transactions,

* See Vol. I. p. 232.

while the volume of aggregate agricultural production, even though influencing the total volume of trade, is not directly a specific indicator as a large part of it does not enter the realm of trade. Some idea of the growth of the economy may be got from the table given below :

Index of Industrial Production

Item	1951	1955	1958	1960	1961	% increase or decrease of (6) over (5)
(1)	(2)	(3)	(4)	(5)	(6)	(7)
General Index	100	122·4	139·7	167·8	180·6	+ 7·6
Coal	100	111·4	132·2	147·6	160 5	+ 8·7
Iron ore	100	116 7	156 3	288·3	313·4	+ 8·7
Sugar	100	143·0	175·6	197·6	244·0	+ 23 5
Tea	100	106·2	113·8	114·3	127·3	+ 11·4
Cotton Textiles	100	111·9	108·9	114·6	116·9	+ 2·0
Jute Textiles	100	118·9	123·9	127·6	111·3	— 12·8
Cement	100	140·4	189·9	238·7	250·1	+ 4·8
Non-ferrous Metal	100	123·7	166·5	338·8	241·4	— 28·7
Iron & Steel	100	113·3	119·1	202·2	261·2	+ 29·2
Transport Equipment	100	129·3	173·7	277·3	301·9	+ 8·9

N. B. 1951—Base year
1960 & 1961—Jan-Oct.

1·4 The contribution of commerce, transport and communication to the National Income* during the period is illustrated by the figures given below :

Year	Total (In Rs. abja)	Percentage
(1)	(3)	(3)
1951-52	17·9	17·9
1955-56	18·8	18·9
1958-59	21·5	17·1
1959-60	22·4	17·3
1960-61	23·6	16·6

N. B. Abja = 100 Crores = 10^9
1960-61—Preliminary estimates

* See detailed tables in Vol I pp 159-162.

An interesting feature noticeable is that the absolute growth of aggregate income from commerce, transport and communications has not kept pace with the growth of total national income as there is decline in its percentage contribution. This is rather a peculiar and paradoxical trend for one would normally have expected this sector to have grown faster than it has in accordance with usual tendency of the tertiary sector to grow rapidly in an expanding industrial economy.

2. **Estimates of Internal Trade and Traffic.**

2·1 Accurate estimates of internal trade are difficult to make due to lack of appropriate statistical data. One could derive some estimates through data relating to traffic carried but in this case also little statistical information is available for goods carried by road or unorganised means of transport. Sometimes an attempt is made to derive figures of internal trade by correlating it to foreign trade; but, this seems highly fallacious, especially in an era of planned economy and rigid import control. In 1940, for instance, internal trade was estimated[75] to be about Rs. 7000 crores while foreign trade was of the order of Rs. 500 crores; but, today a similar ratio between the two could hardly be expected to exist.

2·2 A rapidly developing economy must place large demands on the transportation system of a country. It is necessary to recognise that the demand for transport is not entirely dependent on growth of production, for generally with an increase in the average lead of freight traffic, the total demand on transport is much greater than the increase in production. The Third Five Year Plan[76] gives the following figures of the volume of goods traffic (which is the basic determinant of total internal trade) carried by railways and road transport:—

Year	Railways tons originating	Railways ton miles	Road ton miles	(Millions) Total of (3) & (4)
(1)	(2)	(3)	(4)	(5)
1950-51	91·5	26,980	3,358	30,338
1955-56	114·0	36,434	5,470	41,904
1960-61	154·0	54,700	10,600	65,300
1965-66 (Estimate)	—	96,000	23,350	119,350

75 National Planning Committee.
76. p 538.

It may be clarified that figures in columns (2) & (3) are based on actual traffic carried by Indian railways, those for road transport are only estimates for which suitable assumptions were made regarding utilisation of vehicles as figures of actual volume of traffic in different commodities carried by road transport are not available. The total traffic carried in the country was obviously much larger than those indicated in column (5) above for allowance must be made of the traffic carried by inland waterways, country boats, bullock-carts and other forms of unorganised transport.

2·3 The lessons of the period 1950-1960 have revealed that the demand for transport has risen much faster than either (a) national income, or, (b) production in the major sectors. It has been concluded[77] that:

> "while the national income has increased by about 42 percent, the index of agricultural production has gone up by about 41 percent and that of industrial production by 94 percent, the traffic on the railways measured in ton miles has doubled and that on road transport more than doubled over the period"

2·4 *Future Estimates.* It is difficult to make estimates for the future with any degree of accuracy because of two complicating factors, the trends of which are generally uncertain and difficult to assess *viz.*,

(i) lead of traffic, and,

(ii) cross movements and multiple movements.

The average lead of traffic on the railways is estimated to have increased in the Second Plan period from 292 miles in 1955-56 to 354 miles in 1960-61 and it is estimated to increase still further by the end of the Third Plan to about 390 miles. No precise estimates for Road Transport are available. The *Ad Hoc* Committee on the Automobile Industry assumed (presumably on the basis of the Report of the Chief Engineers on 20-Year Road Development Plan used by the Technical Sub-Committee of the *Ad Hoc* Committee) that the long distance traffic in the country in 1960-61 was 180 million tons and in 1965-66 it would be 280 million tons. From the figures given earlier (vide para 2·2) it seems that the increase in total traffic in ton-miles in 1965-61 over 1960-66 would be about 83%, divided between road and rail, the former getting an increase of about 12%, while the latter's share of

77. Third Five Year Plan, p 539.

increase being about 85%. To this must be added the volume of traffic that would be carried by other means of transport, especially coastal shipping and inland waterways; these, however, at present carry only an insignificant proportion and even by the end of the Third Five Year Plan their contribution is not likely to be of much greater significance.

2·5 The Indian Railways are still the chief carrier of goods traffic in the country, and the Third Five Year Plan continues to rely mainly on the railways as the primary transportation agency of the country, and, this is well borne out by the provision for transport and communications programme in the Third Five Year Plan which is as follows:

(Rs. crores)

Programmes	Provision	
1. Railways	890	
	+350	(contribution from rail way depreciation fund)
	+ 35	(Stores Suspense account)
2. Roads & Road transport	297	
3. Shipping, Inland Water-transport; ports etc.	133	
	+ 20	(ports own resources)
4. Civil Air transport	55	

2·6 The allocations are not based on any detailed estimate of the likely increase in the overall traffic demands in the country as it is not possible to attempt this, *inter alia*, for want of relevant data regarding different means of transport. Thus, for instance, in regard to road transport which is the most important means of transport next to railways, no dependable estimates of traffie according to commodities or according to regions are available. In fact, difficulties of precise estimation of traffic requirements have been frankly recognised in the Third Five Year Plan,[78] which states :

> "In the nature of things the traffic requirement five years hence cannot be calculated very precisely. In the first place, the location of some of the important units in industries like coal and fertilizers is still not definitely known, and it is not possible to forecast precisely the pattern of traffic in these commodities. In the case of the coal

78. p 543.

industry particularly, it is difficult to foresee the exact impact on the average distance of haul of the changes in the pattern of production envisaged in the Third Plan in so far as a substantial part of the production is expected from fields other than the Bengal and Bihar Coalfields.* Secondly, in respect of some important commodities like iron ore and steel, because of increased production within the country, the pattern of future movement may be very different from what it has been in the recent past. Thirdly, ...it is difficult at this stage to define precisely the respective spheres of rail and road transport in the country, although that part of the additional traffic in the Third Plan in respect of which railways and road transport would appear to be competitive, is comparatively small."

In spite of the difficulties, it is necessary, if appropriate transport planning is to be achieved; to work out the total traffic demand in the country corresponding to the targets of production envisaged during the Third Plan period. This has been attempted for rail movement, as statistical data relating to the railways is available in considerable detail.

2·7 In the Third Plan, the Railway Development Programme has been drawn up on the basis of certain estimates of originating traffic likely to be reached in the last year of the Plan *i. e.* 1965-66. Thus the volume of originating traffic is estimated to reach a figure of 245 million tons in 1965-66 against 154 million tons in 1960-61. A broad break up of this traffic as between various commodities as given in the Plan is indicated below.

(million tons)

Commodity	1955-56	1960-61	1965-66	increase in 1965-66 over 1960-61
Steel and raw materials (other than coal for steel plants)	5·09	13·0	34·0	21·0
Coal (includidg coal moved on railways' own account)	35·34	49·5	90·0	40·5
Cement	3·96	6·5	12·0	5·5
General goods including Railway materials excluding coal		18·0	22·5	4·5

*There are little indications so far of this expectation being fulfilled.

Iron ore for export		3·0	11·0*	8 0
All other goods		64·0	75 5	11 5
Total for 'general goods'	69·67	85·0	109·0	24·0
Total	114·06	154·0	245·0	91·0

In regard to the three basic industries, namely iron and steel, coal and cement, calculations of transport requirements are stated to have been made on the basis of the estimated production and the probable location of production units. Thus the estimate of traffic in respect of steel and the raw materials of steel corresponds to production target of 8·3 million tons of finished steel and pig iron. It may be mentioned that for every one million tons of finished steel, roughly about 3·1 million tons of raw materials other than coal and about 2·1 million tons of coal are required to be moved to the steel plants. The estimated traffic in coal of 90 million tons is based on a production target of 97 million tons, the difference of 7 million tons being explained by consumption at collieries and the anticipated movement of coal by means of transport other than the railways. The estimated cement traffic of 12 million tons is based on the estimate of production of cement of 13 million tons in 1965-66. As regards the provision for traffic in general goods in the Third Plan, the estimate includes 22·5 million tons of railway material, 11 million tons of iron ore and 75.5 million tons of other goods making a total of 102 million tons. The Third Plan provides for a total increase in traffic in general goods to the extent of 29 per cent (from 85·0 million tons in 1960-61 to 109·0 million tons in 1965-66) against 24 per cent increase in the Second Plan (from 69·67 million tons in 1955-56 to 95·0 million tons in 1960-61). Excluding iron ore traffic which has been specifically provided for in the Third Plan, the Third Plan provides for an increase of 19·5 per cent in general goods traffic against about the same percentage increase during the the Second Plan.[79]

3. Economic Growth and Demand for Transportation.

3·1 The problem of the transport requirements of a country assume special significance in the process of economic development. It is generally recognised that the need for transport increases continuously during the process of economic growth. It has been pointed out that :

> "As the economy produces more, a larger volume of materials must be brought together to provide the

*Includes capacity of 4 million tons of exports from Bailadilla area through Viskhapatnam to be reached in 1966.

79 See Third Five Yeer Plan, p 542

> necessary ingredients, and larger quantities are distributed to consumers. The increase in volume may also be accompanied by an extension of the area from which materials are assembled, as well as the area in which the increased production is marketed. The number of goods exchanged will multiply with increasing specialisation, and rising incomes will add to the variety of goods that will be demanded. In a word, increasing economic activity involves, and depends to a large extent, on increasing mobility."

It is obviously necessary to recognise that a developing economy logically involves an expansion of production and consumption, and that this must intensify the importance of transport. Further, in India there is bound to be a continuous process of converting more and more of the economy into the market economy (as distinguished from self-consumption) which in turn would add to the needs of transport. Finally, planning in India has deliberately adopted a policy of increasing emphasis on regional development which will probably change fundamentally the relative structure of demand for transport.

3·2 In view of the various considerations indicated, it is generally believed that in a planned economy of the type we have in India, it is both necessary and desirable to avoid a close balancing between transport requirements and provision of transport services, and, a margin should be provided to permit of adjustment to the concept of a mixed economy. Logically, therefore, transport facilities planned, should be somewhat in excess of the requirements anticipated. This view was recognised by the Indian Railway Freight Structure Enquiry Committee (1955-57) who observed,

> "In an ordinary *laissez faire* economy, the failure to provide in time adequate transport may not be as disastrous as in a planned economy, which involves rationing of resources and dovetailing of one part of the economy with the other by the planners. This fine balancing is the very heart of planned economy. Ordinary forces of competition and entrepreneurial speculation, which is at once the price paid for and the self-acting corrective of free economies, may no longer have full play. In view, however, of the fact that the private sector will have an important place in the economy, the aim should be to provide adequate transport as

> quickly as possible with a reasonable margin, so that, in the planned progress of the country, transport is not allowed to lag behind present and future development. The resources employed in providing some cushion in transport capacity should not be considered as wastage and should really be treated as an insurance against transport bottlenecks and an inducement to enterprise."

The committee on Transport Policy and Co-ordination,[80] known as the Neogy Committee, attempted certain forecasts of traffic demands in India by making future projections of traffic on the basis of past trends in the relationship between traffic, national income, and, industrial and agricultural production. It is, however, doubtful how far the approach adopted was likely to provide satisfactory results, for as has been pointed out rightly in the Third Five Year Plan (see para 2·6 above) the "uncertain" factors are too many to permit of any close correlationship being established with evidence culled from past trends. This is further illustrated by the fact of large scale transport shortages in the beginning of the third plan period even though the Third Plan makes provision for a somewhat higher transport capacity per unit of production than the Second Plan; yet, inspite of this larger provision it has been recognised[81] that "........there is a general shortage of transport in the country, which is likely to continue for some time........."

4. Regional Development in relation to Trade and Transport

4·1 Even though planning in India is a national process, it has specifically recognised as one of its major aims balanced development of different parts of the country with extension of the benefits of economic progress to the less developed regions so as to achieve widespread diffusion of industry. It is clear that such a policy must lead to an increase in the quantum of trade for a given quantum of production. It must also lead to a larger pressure on transport for cross haulage and multiple movements must necessarily follow unless, as in the U. S. S. R., the relatively undeveloped areas are also sources of raw material and fuel. The concept of removing the uneveness of economic activity is, however, a concept of wider economic policy, and, will have to be adopted even when it makes larger demands on transport for transport is a means, not an end in itself. Since the new

80. See Preliminary Report pp 116-118 & Appendix 21.
81. Third Five Year Plan, p. 540.

production units cannot always be built closer to sources of raw materials and the centres of consumption, cross-hauls, multiple movements and long leads cannot be avoided completely, but the strain that such dispersal of industries may put on the transport system of the country and the larger investment that may consequently be required may be more than made good by taking advantage of other important fectors such as labour supply or existing social capital, to say nothing of the non-measurable advantages of comprehensive economic development and increases in aggregate welfare.

4·2 Balanced regional development, involving as it does dispersal of industrial location is not necessarily inconsistent with the objective of a high and sustained rate of growth for India is a large country with extensive natural resources. Further, economic growth of underdeveloped areas often creates for itself its own market through rising incomes.

4·3 Approach to Balanced Regional Development in India in the Five Year Plans. The approach to balanced regional development in the country was set out in the Second Five Year Plan as follows :

> "In any comprehensive plan of development, it is axiomatic that the special needs of the less developed areas should receive due attention. The pattern of investment must be so devised as to lead to balanced regional development.........The problem has to be approached in a variety of ways. In the first place the National Development Council has recommended programmes for setting up decentralised industrial production. Secondly, it has been suggested that in the location of new enterprises whether public or private, consideration should be given to the need for developing a balanced economy for different parts of the country. Some industries have to be located in particular areas in view of the availability of the necessary raw materials or other natural resources. But, there are other industries in regard to the location of which, on economic considerations, there is a field of choice. Often, the disadvantages of comparative cost are only a reflection of the lack of basic development. Once this is taken in hand, the initial handicaps progressively disappear. A wide diffusion of development nucleii is essential from this point of view. Thirdly, steps have to be taken to promote greater mobility of labour between different parts of the country, and to organise schemes of migration and settlement

from more to less densely populated areas. The National Development Council recommended that there should be continuous study of the problem of diminishing regional disparities and a suitable set of indicators for regional development evolved......"

(quoted from the Second Five Year Plan—pages 36-37)

The Second Five Year Plan embodied the following main policies and programmes to promote regional growth :

(1) priority to be given to programmes like agriculture, community development, irrigation, specially minor irrigation, local development works, etc. which spread over the entire area within the shortest possible time;

(2) provision of facilities such as power, water supply, transport and communnications, training institutions etc. in areas which were lagging behind industrially or where there was greater need for providing opportunities for employment;

(3) programmes for the expansion of village and small industries;

(4) in the location of new enterprises, whether public or private, consideration to be given to the need for developing a balanced economy in different parts of the country. In particular, this aspect was to be kept in view where the location of an industry was not determined almost entirely by the availability of raw materials or other natural resources."

(quoted from the Third Five Year Plan, pages 142-144)

4·4 The Third Five Year Plan also embodies this approach to balanced regional development. According to the Plan :

"Balanced development of different parts of the country, extension of the benefits of economic progress to the less developed regions and widespread diffusion of industry are among the major aims of planned development. Successive Five Year Plans seek to realise these aims in larger measure."

4·5 Referring to the need for decentralisation in industrial development, the Third Plan states as follows :

"The general approach has to be to avoid further concentration of industrial activity in areas where considerable development has already taken place or has been planned, but expansion in existing

> industries in such areas cannot, of course, be ruled out if it leads to greater economies in production. Similarly, as far as possible, care must be taken to set up new industries a way from large and congested cities."

Some of the main programmes contemplated for achieving balanced regional development are broadly referred to in the Third Plan as follows :

> "The growth potential of each region should be fully developed, but the precise manner in which this goal is achieved and the stages of growth will not be identical. Some regional factors, such as those connected with physical features and geographical location, cannot be easily altered, but there are others which can be influenced by raising levels of education and skill, developing power and, generally, by applying science and technology on a larger scale. Large scale industries, specially basic and heavy industries, frequently serve as a spearhead of intensive and broad-based development. However, not all regions can offer equally favourable conditions for the development of industry. It is also possible to over-estimate the significance of the location of large industrial units in relation to the living standards of the bulk of the population."

4·6 According to the Third Plan, some of the most important programmes in the Plan fall necessarily within the Plans of States. In drawing up these Plans, the broad objectives have been to enable each State to contribute its best towards increasing agricultural production, to secure the largest measure of increase in income and employment feasible, to develop social and, in particular, elementary education, water supply and sanitation, and health services in the rural areas and to raise the levels of living for the less developed areas.

4·7 The Plan further contemplates the setting up of "industrial development areas" in backward regions. In such regions in selected areas basic facilities like power, water and communications are to be provided, and factory sites developed and offered for sale or on long lease to prospective entrepreneurs. This scheme is intended primarily to promote medium-sized industries, but it is anticipated that along with these, there will be wider scope for establishing small-scale industries, specially those of an ancillary character.

5. The Indian Railways.

5·1 The first railway line was constructed in India more than a hundred years ago, primarily on considerations of military necessity. The maintenance and expansion of British authority in India demanded an inexpensive and expiditious mode of transport for the movement of troops and military equipment. The exploitation of the natural resources of the country to assist the expansion of British industrial production was also an additional consideration. Whatever may have been the origin, the railways gradually came to be symbolised with the growth of trade and commerce, and, have been the most important single instrument of national economic integration and development.

5·2 Initially the railways were company-managed with generous guarantee from Government of return on capital invested. The system, however, entered on its most revolutionary phase with the report of the Acworth Committee after the first World War who advocated the gradual adoption of a policy of State enterprise in the field of future railway expansion. The first steps in this direction were taken in 1925 with the termination of the managing agency arrangements in regard to the East Indian and the G.I.P. Railways; but the final phase of nationalisation was not completed till 1944 when the last managing agency system was determined. The process of nationalisation was, however, fully realised only after independence, when the integration of the Indian States with the Indian Union and the assumption of federal functions by the Government of India took place. It was only in 1953 that the establishment of a nationalised and unified railway undertaking for the country was realised and the Indian Railways became the nation's largest industrial undertaking. The history of railways in India is a history of progressive Government participation in a commercial enterprise. It began with the giving of financial guarantees to the companies which undertook construction of railway lines, and ended with direct management, with an intervening period when Government were directly constructing and administering a part of the railway system side by side with the private companies.

5·3 *Social Aspects of Railway Working*. It is necessary to recognise that even though it is the largest single industrial undertaking, it would be a mistake to regard the Indian Railways as a commercial proposition, pure and simple. In fact in the past state policy in regard to the development of railways has been guided not so much by purely commercial considerations as by the desire to promote general economic

interests of the various regions in the country and by the necessity, often unavoidable, of using the railways for furthering social, political and strategic purposes from time to time. The railways, therefore, have certain social obligations for though a commercial concern, they are hardly a commercial concern in the conventional and narrow sense. Broadly speaking, the railways are expected to achieve many things, commercial and non-commercial, some of which are not always consistent with one another. Thus, the Indian Railways are today expected to :

(1) make sizeable contributions to the resources of the Third Plan, by providing a certain portion of the finance for their development ;

(2) undertake a definite obligation to make contributions to the General Revenues, the terms of which are to be prescribed by the Railway Conventions Committee ;

(3) assist, through appropriate differential rating system, certain lines of trade and certain economic objectives desired to be pursued by Government in the national interest, e.g., cheap movement of food-grains, coal and other raw materials ;

(4) avoid any personal preference or discrimination, for the Railway Act enjoins that

"whenever it is shown that a railway administration charges one trader or a class of traders or the traders in any local area lower rates for the same or similar animals or goods, or lower rates for the same or similar services, than it charges to other traders or classes of traders, or to the traders in another local area, the burden of proving that such lower charge does not amount to an undue preference shall lie on the railway administration" ;

(5) discharge the obligations of a common carrier which involves

(a) the obligation to carry traffic that may be offered, and

(b) liability for claims for compensation ;

(6) provide uneconomic lines as links to "civilization", and, maintain cheaply suburban (or what are known as commuter) services in large cities to avoid overcrowding in congested residential areas ;

(7) ensure safety, regularity and reliability of service as per scheduled obligations ; and

(8) obey Government direction, given under Section 27-A of the Indian Railways Act, to give preference to the transport of such goods or class of goods, as may be specified by it

It is apparent that some of the above "social obligations" must necessarily mean financial losses which a purely commercial organisation would hardly voluntarily undertake. It has, therefore, sometimes been urged that the railways should be freed of such non-commercial obligations, or alternatively, the cost of such public service obligations should be reimbursed to them—a view with which many would find it difficult to agree as long as the railways are State-owned and directly managed by the Government with the Railway Board performing the dual functions of the Chief Administrative Authority of the Indian Railways and the Secretariat of the Minister for Railways functioning like any other Ministery of the Government of India and exercising all the powers of the Central Government in respect of regulation, construction, maintenance and operation of the railways.

5·4 Review of Rail Performance and progress of Rail ways.

5·4·1 *Railway route mileage.* It must be frankly admitted that the density of railway mileage in India is very low, and, compared to some of the advanced countries of the world, extremely unsatisfactory. International comparisons are apt to be somewhat misleading for basic conditions of terrain, economic prosperity and, even, propensity to travel may differ widely from country to country ; but, in spite of these limitations, the backward stage of railway development in India is brought out by the comparative figures given blow :

Country	Per one Kilometre of Railway Track	
	Area (Square Kilometre)	Population (number of persons)
India	50	5,000
U. S. A.	12·8	277
U. K.	7·5	1,613
Japan	10·6	2,588
France	13·9	1,075
West Germany	8·1	1,613

Source : Preliminary Report of the Neogy Committee
N. B. See also Vol. I, p. 117

There are many regions in India at present without railways where there would be urgent need for opening up railway lines for the railways are the chief agencies for

promoting general economic development. The pace of extension of railway mileage has also not been satisfactory since over the 10 year period from 1951-52 to 1960-61, the total mileage added was only 1200, a sizeable portion of which was on account of the lines which were dismantled during the war but restored under the first two plans.

Progress of railway mileage

Year	Open mileage at the end of the year	Mileage added
1948-49	33,861	
1950-51	34,079	+218
1955-56	34,735	+656
1956-57	34,744	+9
1957-58	34,889	+145
1958-59	35,081	+192

Source : Preliminary Report of the Neogy Committee.

The railway route mileage figures for the whole of India hardly gives any adequate idea as to regional differences in this respect for obviously it could be no consolation to Jammu & Kashmir, where there is no railway line, to know that India as a whole has nearly 35,000 miles of it. While it must be recognised that equal, or even comparable to area, railway route mileage for the different States cannot be a deliberately adopted policy for laying railway lines, existence of wide diversity in this respect may react unfavourably on the growth of trade and commerce in the country and may even obstruct realisation of the accepted policy of balanced regional development. The table given below illustrates the State-wise distribution of railway route mileage in India :

Railway route mileage.

State	Broad Gauge	Metre Gauge	Narrow Gauge	Total
(1)	(2)	(3)	(4)	(5)
Andhra Pradesh	1600	1184	23	2807
Assam	...	1088	...	1088
Bihar	1623	1221	79	2923
Bombay	2232	2692	1395	6319
Kerala	357	110	...	467
Madhya Pradesh	2059	267	714	3040
Madras	520	1684	...	2204
Mysore	300	1281	96	1677
Orissa	734	...	104	838
Punjab	1666	510	140	2316
Rajasthan	404	2783	54	3241

(1)	(2)	(3)	(4)	(5)
Uttar Pradesh	3214	2045	2	5261
West Bengal	1375	424	107	1906
Union Territories	58	16	21	95
All-India (Total)	16142	15305	2735	34182

N. B. Figures as on 31st March 1956
Source : Second Finance Commission Report.

Subsequent comparable figures are a little difficult to construct due to the increasing trend of railway statistics to give only All-India and zonal figures; but the relative position could hardly have changed very much as the total new mileage added since 1956 was only about 650 miles, and, as, apart from the bifurcation of Bombay and the formation of the States of Maharashtra and Gujerat, there have been no significant readjustments of State boundaries.

5·4·2 *Capital Structure.* Investment: At the end of March, 1960 the total investment on all railways in India, including non-government railways and lines under construction, from capital (loan account) as well as railways' own resources, amounted to Rs. 17,39·12 crores of which Rs. 17,32·65 crores represented the investment on Government Railways, financed from different sources as under :

Provisional figures of total investment on Indian Government Railways from different sources.

	As on 31st March 1959*	As on 31st March 1960†
	(Rupees in lakhs)	
Capital-at-Charge (loan account inclusive of premia paid on the purchase of certain Companies' Railways). . . .	13,56,59	14,32,28
Depreciation Reseve Fund (on improvement of assets replaced)	71,92*	82,85
Development Fund	1,19,98*	1,43,08
Revenue	63,21*	74,44
Total investment . . .	16,11,70*	17,32,65

*Revised figures. †Provisional figures.

The balance of Rs. 6·47 crores was the capital raised by companies and district boards.

The sterling liabilities incurred in the purchase of railways have all been liquidated by general revenues by 31st March, 1959.

The investment on Government Railways during the year 1959-60 amounted to Rs. 120·85 crores as detailed below:

	(Rs. in lakhs)
Capital (loan account)	74,69
Depreciation Reserve Fund (on improvement of assets replaced)	10,84*
Development Fund	24,12*
Revenue	11,20*
Total	1,20,85

Source : C.S.O.

*Provisional figures.

The capital outlay on non-Government Railways during 1959-60 was Rs. 16·32 lakhs only.

5·4·3 *Goods Traffic Carried.* Much of the trade of a country follows from mobility and transportation, for the proportion of production that is consumed locally *i.e*, without involving any movement through rail or other long-distance means of traffic is generally extremely small. It is, of course, true that in India a fairly large part of the agricultural produce is carried from the cultivator's lands to the nearest *mandi* in bullock carts, so that a part of this trade is obviously not covered by statistics (such as is available in our country) of traffic carried through organised means of transport. It has been pointed out earlier that data relating to railway traffic alone is fairly comprehensively available, and, as the railways are indisputably the major carriers in the country, the quantities moved by rail of the different commodities is generally connected directly with the amounts of their internal production. In some cases, however, imports and exports have important bearings on rail movement. In the case of foodgrains, for instance, large imports under the American P.L. 480 Aid make the demand for movement heavy. The movement of metallic ores is substantially influenced by export demands, quite apart from the direct effect of the growth of ore-consuming industries within the country, *i.e*, in this case the extent of rail movement would be greater than that indicated by the expansion of the steel industry and non-ferrous industries within the country. Similarly, in the case of oilseeds, rail-movement is affected more by export demands than by its internal trade. It is also necessary to recognise that for many commodities, e.g. cement, sugar, paper, iron and steel etc, the process of retail distribution makes for cross movements, involving double or even treble carriage by rail. The location of an industry has an important effect on demands for rail transportation, for if the consuming industry is located near the raw-material source, as for instance sugar and sugarcane, only a small percentage of the raw material

would move by rail. The factors determining the quantum of movement by rail for any particular commodity are, therefore, complex and varied, and, no simple correlation between production, rail-movement and trade can be easily established. It is, however, still important to study the pattern of rail movement, partly with a view to understanding whether rail freight traffic has kept pace with the increasing industrial and agricultural production, but mainly as providing the basic indicators for planning railway expansion and investment policy *vis a vis* expansion of road transport and other means of transport. The past trends in the realm of rail movement have been analysed below :—

TABLE I

Statement showing production, imports and rail-movement of principal commodities during the Second Plan period.

(Figures in 000 tons)

Commodity	1956-57	1957-58	1958-59	1959-60	1960-61
(1)	(2)	(3)	(4)	(5)	(6)
1. Coal					
(a) Production	39,434	43,500	45,300	47,028	53,000
(b) Rail Movement	38,158	40,518	43,252	44,616	49,847
%of (b) to (a)	96·8	93·1	95·9	94·9	94·05
2. Cement					
(a) Production	4,929	5,602	6,062	6,828	7,750
(b) Rail Movement	4,291	5,077	5,012	6,058	6,752
%of (b) to (a)	87·1	90·6	82·7	88·7	87·12
3. Iron & Steel					
(a) Production and Imports	3,637	3,402	2,971	3,704	3,704*
(b) Rail Movement	4,237	4,861	5,595	6,602	6,602*
%of (b) to (a)	117·0	142·9	188·3	178·2	178·2
4. Iron & other ores					
(a) Production	5,744	5,973	6,723	8,677	12,500
(b) Rail Movement	4,630	5,351	5,807	8,558	10,589
%of (b) to (a)	80·7	89·6	86·4	98·6	83·2
5. Manganese ore					
(a) Production	1,687	1,650	1,200	1,168	1,800

(1)	(2)	(3)	(4)	(5)	(6)
(b) Rail Move-	1,647	1,620	974	1,173	1,680
% of (b) to (a)	97·6	98·2	81·2	100·4	93·35
6. Foodgrains					
(a) Production and Imports	70,168	66,091	76,673	75,557	75,557*
(b) Rail Movement	9,685	11,076	11,945	12,287	12,287*
% of (b) to (a)	13·80	16·76	15·58	16·3	16·3
7. Oilseeds					
(a) Production	6,176	6,051	6,919	6,352	6,992
(b) Rail Movement	16,42	1,641	1,497	1,467	1,890
% of (b) to (a)	26·59	27·1	21·6	23·1	27·03
8. Sugar Cane					
(a) Production	66,998	68,019	70,456	75.038	75,038*
(b) Rail Movement	3,712	3,324	2,627	3,141	3,141*
% of (b) to (a)	5·54	4·89	3·73	4·18	4·18
9. Sugar					
(a) Production	2,008	1,957	1,918	2,410	2,450
(b) Rail Movement	1,536	1,516	1,382	1,354	1,847
% of (b) to (a)	76·49	77·46	72·05	56·2	75·39
10. Raw Cotton					
(a) Production and Imports	966	914	892	782	941
(b) Rail Movement	703	680	541	531	709
% of (b) to (a)	84·8	81·7	62·47	67·9	75·32
11. Cotton Manufactures					
(a) Production	736	770	727	738	745
(b) Rail Movement	482	484	430	394	470
% of (b) to (a)	65·5	62·9	59·1	53·4	63·15
12. Jute Raw					
(a) Production	766	724	925	894	914
(b) Rail Movement	720	688	728	799	802
% of (b) to (a)	94·0	95·0	78·7	89·4	85·0
13. Jute Manufactures					
(a) Production	1,093	1,030	1,062	1,051	1,100
(b) Rail Movement	269	259	261	253	277
% of (b) to (a)	24·61	25·15	24·58	24·07	25·16
14. Salt					
(a) Production	3,265	3,620	4,135	3,128	4,400

(1)	(2)	(3)	(4)	(5)	(6)
(b) Rail Movement	1,715	1,880	1,781	1,952	2,313
% of (b) to (a)	52·53	51·83	43·07	62·4	52·56
15. Tea					
(a) Production	298	303	316	316	324
(b) Rail Movement	274	297	285	260	304
% of (b) to (a)	91·95	98·00	90·2	82·3	93·9
16. Paper & Paper Board					
(a) Production and Imports	323	333	332	366	360
(b) Rail Movement	261	306	364	411	310
% of (b) to (a)	82·5	92·0	109·6	89·1	86·24
Total for 16 Commodities					
(a) Production	2,08,228	2,11,786	2,26,611	2,34,037	2,47,605
(b) Rail Movement	73,968	79,578	82,663	89,856	99,820
% of (b) to (a)	35·52	37·57	36·48	38·39	40·3

*The figures for 1960-61 have been assumed to be the same as in 1959-60.

Source: A Review of the Performance of Indian Government Railways—issued by the Railway Board.

On the basis of Table I, one could construct an index showing the trends in the past between production and rail-movement. This is shown below:—

TABLE II

Statement showing Index of increase in Production and Rail Movement of a few Principal Commodities during Second Plan period

Commodity	1956-57 (Base=100)	1957-58	1958-59	1959-60	1960-61
(1)	(2)	(3)	(4)	(5)	(6)
1. Coal—					
Produetion	100	110·3	114·9	119·3	134·4
Rail Movement	100	106·2	113·3	116·9	130·6
2. Cement—					
Produttion	100	113·7	123·0	138·5	157·2
Rail Movement	100	118·3	116·8	141·2	157·4
3. Iron & Steel—					
Production	100	93·5	81·7	101·8	101·8

(1)	(2)	(3)	(4)	(5)	(6)
Rail Movement	100	114·7	132·1	155·8	155·8
4. Iron & other ores—					
Production	100	104·0	117·0	151·1	217·6
Rail Movement	100	115·6	125·4	184·8	228·7
5. Manganese—					
Production	100	97·8	71·1	69·2	106·7
Rail Movement	100	98·4	59·1	71·2	102·0
6. Foodgrains—					
Production	100	94·2	109·3	107·7	107·7
Rail Movement	100	114·4	123·3	126·9	126·9
7. Oilseeds—					
Production	100	98·0	112·0	102·8	113·2
Rail Movement	100	100·0	91·2	89·3	115·1
8. Sugar Cane—					
Production	100	101·5	105·2	112·0	112·0
Rail Movement	100	89·5	70·8	84·6	84·6
9. Sugar—					
Production	100	97·5	95·5	120·0	122·0
Rail Movement	100	98·7	90·0	88·2	122·3
10. Raw Cotton—					
Production and imports	100	94 6	92·3	81·0	97·4
Rail Movement	100	96·7	77·0	75·5	100 0
11. Cotton Manufactures—					
Production	100	104·6	98·8	100·3	101·2
Rail Movement	100	100·4	89·2	81·7	97·5

The above can now be used for estimating the possible future relationship between the two—subject, of course, to the limitations pointed out earlier, and, by applying the ratio between the two indices to the targets of production in the Third Plan one can make rough (but perhaps not too satisfactory) estimates of future trends of rail movement.

(TABLE III)

Statement showing Production Targets in 1965-69; Increases in Production and Rail Movementduring the Second Plan, and Estimates of Rail Movement in 1965-66.

Commodity	Production targets in 1965-66 (000 tons)	Increase in production in 1960-61 with 1956-57 as base = 100	Increase in rail movement for 1960-61 with 1956-57 as base = 100	Index of production in 1965-66 with 1656-57 as base	Tonnage of of rail movement for 1965-66 (000 tons) †
(1)	(2)	(3)	(4)	(5)	(6)
1. Coal	97,000	134·4	130·6	246·0	91,767
2. Cement	13,000	157·2	157·4	263·7	11,368

(1)	(2)	(3)	(4)	(5)	(6)
3. Iron & Steel*	9,400	101·8	155·8	258·5	16,784
4. Iron & other ores	30,000	217·6	228·7	403·7	27,723
5. Manganese ores		106·7	102·0		
6. Foodgrains*	105,400	107·8	126·9	150·2	17,083
7. Oilseeds	9,800	113·2	115·1	158·7	3,012
8. Sugar Cane	100,000	112·0	84·6	149·3	4,206
9. Sugar	3,500	122·0	120·3	174·3	3,042
10. Cotton	1,361	97·41	100·83	141·0	1,032
11. Cotton Manufactures	1,300	101·2	97·51	168·0	786
12. Jute Raw	1,528	123·5	111·4	199·5	1,300
13. Jute Manufactures	1,300	100·6	102·97	118·9	326
14. Salt	5,400	134·8	134·9	165·4	2,830
15. Tea	402	108·7	111·0	134·9	377
16. Paper and Paper Boards	772	111·5	111·6	239·0	644
					182.280
Total :	380,163				
		Estimates forgeneral goods			71,900
			Total traffic		254,18 0

*Figures include production and imports; imports at the end of the Third Plan assumed at the level of 1959-60, except in case of foodgrains which includes imports anticipated for the year 1964-65.

† The figures in column (6) have been worked out as follows:—

$\frac{\text{Col.4}}{\text{Col.3}} \times \frac{\text{Col.5}}{100} \times$ Rail Movement of the base year i.e. 1956-57.

It is not claimed that the above analysis gives substantially better results than alternative estimates but it does show that some estimates can be made, though one must recognise that the future does not always repeat the past.

5·5 *National Finances and the Railways.* The Indian Railways are at present not merely solvent but are making a sizeable contribution to the resources of the country. Reviewing the position in 1953-54, the Taxation Enquiry Commission[82] concluded that "on the whole, it might be said, the Railways have been a productive enterprise of the first order; apart from their contribution to the strength of the national economy, they have given a steady, though modest, support to national finances." Throughout the last decade the Central Government have secured a steady net revenue receipt from railways as indicated below :

82. Vol I. p. 174:

(In Rs. Lakhs)

Year	Revenue Receipt of the Centre from Railways (net)
1950-51	6,50
1951-52	6,93
1955-56	5,80
1956-57	5,86
1957-58	6,29
1958-59	6,26
1959-60	5,63
1960 61 (R. E.)	5,06
1961-62 (B. E.)	21,29

It would appear that upto 1960-61, there has been no sizeable expansion – in fact there is a slight decline; and, considering the large expansion in the total revenues of the Central Government, the percentage contribution of the railways has obviously been on the decline.* The railways however, are a commercial undertaking and appropriate replacements and expansions are a legitimate expectation from its own earnings. The present arrangements provide for

(i) a Depreciation Reserve Fund for replacement requirements, and

(ii) a Development Fund for financing all works of an unremunerative nature like

   (a) passenger amenities,
   (b) labour welfare,
   (c) expensive unremunerative operating improvements
   (d) new lines and projects which are necessary but unremunerative.

So far as replacements are concerned, it would appear that the railways have carried a heavy back-log of overaged assets, a large part of which were overdue for replacement. The result has been that the contributions made by the railways to the Depreciation Reserve Fund have proved inadequate for providing fully for the replacement requirements at the prevailing high prices, and, the balance in the fund has been continuously on the decline. It would appear, if these trends continue, that the balance in the fund which

*See Vol I, p. 372.

was Rs. 100·69 crores on 1st April 1955, and which was reduced to practically an insignificant amount at the beginning of the Third Five Year Plan, would hardly be available for drawing upon with the result that current replacements may have to be wholly financed out of current appropriations. The position regarding the Development Fund has been almost identical and withdrawals have been much higher than appropriations so that the railways had to resort to loans from General Revenues to the extent indicated below to meet their commitments :

1958-59	Rs. 10.98 crores
1959-60	Rs. 14.85 ,,
1960-61	Rs. 7·63 ,,

It is obvious that these trends are not such as to contribute to a sense of optimism in a country embarking on large scale planning, and, the Third Five Year Plan,[83] therefore, expresses the hope that "*prima facie*, it is desirable that financially the Indian Railways should not take the downward path followed by the railway systems in some other countries."

5·6 Railway Finances—A Snmmary of Trends.

(Figures in Rs. Crores)

Item	1950-51	1955-56	1957-58	1959-60	1960-61 (R.E)	1961-62 (B.E)
(1)	(2)	(3)	(4)	(5)	(6)	(7)
1. Capital at charge.	827·04	968·98	1,222·44	1,432·28	1,559·37	1,740·19
2. Gross Traffic Receipts	263·01	316·29	379·78	422·34	458·00	499·02
3. Total Expenses	215·45	265·95	321·99	347·78	387·31	412·54
4. Net Revenue (2—3)	47·56	50·34	57·78	74·56	70·69	86·48
5. Dividend to General Revenues,	32·51	36·12	44·40	54·43	56 66	77·84

83 p. 541 ; see also Preliminary Report of the Committee on Transport Policy and Coordination, Ch. IX.

(1)	(2)	(3)	(4)	(5)	(6)	(7)
of which contribution in excess of interest charges	6·50	5·80	6·29	5.72	5·61	N.A.
6. Surplus (4—5)	15·05	14·22	13·38	20·13	14·03	8·64
7. Appropriations to						
(a) Development Fund	10·00	7·08	13·38	20·13	14·03	8·64
(b) Revenue Reserve fund	5·05	7·14	—	—	—	—

Source : Reserve Bank of India.

It may be pointed out that the sharp rise in the contribution to General Revenues in 1961-62 is mainly on account of the payment of Rs. 12·5 crores in lieu of tax on Railway passenger fares[84] and partly on account of the higher rate of dividend payable from 1961-62 onwards—the rate having been raised from 4 *percent* on the capital at charge to Rs. 4·25 *percent*.

6. Roads and Road Transport.

6·1 *The Constitutional position.* The earlier Government of India Act, 1935 provided that all matters relating to roads were in the Provincial List. Historically, therefore, the sphere of influence of the State Governments in regard to roads was unrestricted till the Constitution of India was promulgated after independence. Under it, 'highways' declared by or under law made by Parliament to be national highways are included in the Union List as item 23 of List I of the Seventh Schedule. The Union Government are, therefore, responsible for the construction and maintenance of such highways, and, have to shoulder the financial liability for the development and maintenane of highways declared to be national highways under a Law enacted by Parliament in 1956. So far as mechanised road transport is concerned, it is included in the Concurrent List being item 35 of List III of the Seventh Schedule. The executive authority for subjects in the Concurrent List lies with the State Governments, except that Article 73

84. See Report of the Third Finance (1961) Commission paras 24—25.

of the Constitution lays down that the Union Government has executive powers in respect of all matters in the Concurrent List only if this is expressly provided for in the Constitution or in any law made by Parliament. In regard to road transport the executive authority rests at present with the State Governments. It is sometimes argued[85] that even though, in general, road transport is exclusively within the jurisdiction of the State Government, interstate transport would be a part of the responsibility of the Central Government in view of entry No. 42 of List I of the Seventh Schedule which makes "Inter-State Trade and Commerce" a Union subject. The view is based on the theory that the term 'commerce' has a wide connotation and includes transport and communications. Whatever may be the legal position, from the point of view of availability of resources for the Third Five Year Plan,[86] it has been frankly acknowledged that "A large part of the road construction programme falls within the purview of the State Governments," and, that "The Programmes in the central sector provide mainly for the improvement of the existing National Highways system." If, therefore, road development is to be the responsibility of the State Governments, it is difficult to visualize an arrangement whereby interstate transport should come within the purview of Central functions unless such transport were to use only the national highways, an arrangement not likely to promote fully national economic development at a rapid pace.

6·2 *Road Development in India.** The road development programmes in the last two plans were based on a 20 year road development programme drawn up as far back as 1943. The 1943 programme, known commonly as the 'Nagpur Plan', envisaged completion of a total length of 123,000 miles of surfaced roads and 208,000 miles of unsurfaced roads, as applied to post-partition India. While it is true that for India as a whole the targets envisaged in the Nagpur Plan have been exceeded, the position of road-availability in the different States is not uniform, nor does it seem that the existing length available is adequate, at least in some of the more under-developed areas, to promote the required degree of mobility essential for rapid economic development. It is generally agreed that good communications are the basis of efficient marketability which, in turn, is the primary incentive for increased production. Roads are the link between the producer and the consumer, and, more important than

85. Preliminary Report of the Committee on Transport Policy and Co-ordination, p. 32.

86. P. 550, 551

* See Vol I, Ch. 1, Table 23 for Statewise Growth of surfaced roads.

highways parallel to the railways, are the roads that link the primary producer to the rail-head which caters to long-distance urban markets. Roads are the media through which progress can be brought to the interior, and, the mobility provided by the roads assists in a general raising of living standards—economic, social and cultural. It is a mistake—at least, a narrow short-sighted view—to link the extent of surfaced roads either to the number of vehicles available or to the volume of production, for such approaches neglect the wider values of providing links between developed and un-developed areas. It is necessary to recognise that :

(i) the wider the geographical area and the greater the variety of resource endowments in various regions, the greater is the need for good communication for bringing together the wealth of the different parts of the country to promote economic development. In short, the wider the locational discrepancy in resource endowment in a country, the greater is the need for transportation ;

(ii) the more agricultural an area, the greater is the need for a net-work of roads to link the small producer to the organised markets, for rail-link can generally benefit only organised industries ;

(iii) economic development, road communications and the extension of transport net-work are mutually inter-dependent for communication widens the market, provides economies that generate a process of economic development which in turn stimulates the need for a more extensive transport system.

The road mileage position in India in relation to area or population is extremely unsatisfactory, and, compared to the more advanced countries of the world, indicates a level which is perhaps lower than would be justified even by the deviation of our per capita national income from those of the other countries. The table given on next page attempts a study of international comparisons* (which, it may be pointed out, must be taken with caution in view of the many difficulties in such comparisons) :—

* See Vol I. p. 115.

Country	Road Mileage		Per Capita Income in U.S. Dollars
	Per 100 sq. miles of area	Per one Lakh of population	
(1)	(2)	(3)	(4)
India	26	85	63
France	338	1,630	869
Germany (West)	169	314	1,006
Italy	106	256	454
Japan	63	100	299
U.K.	215	382	1,083
U.S.A.	114	2,018	2,311

It is obvious that there is a great need for the extension of road mileage in the country, particularly in those states and regions which are considerably below the All-India average.* Further, apart from mere extension of mileage, it is necessary to improve quality so as to enable heavier goods-vehicles to operate, complete missing links and bridges, and, integrate the entire system with a net-work of feeder roads from the interior to the rail-heads.

6·3 *Road Development in the Third Plan*. A plan has recently been drawn up by the Chief Engineers of the State and the Central Governments laying down the broad pattern of a twenty-year road development programme for the period 1961-81. The Third Five Year Plan has adopted this programme, and, seeks to achieve the following objectives :—

(a) no village in a developed and agricultural area should remain more than 4 miles from a metalled road ;

(b) no village of the above type should be more than $1\frac{1}{2}$ miles from any type of road ;

(c) account should be taken of the special requirements of undeveloped and under-developed areas ;

(d) missing bridges are to be provided ;

(e) quality of metalled roads are to be improved to make them suitable for heavy traffic ;

(f) rural roads should be improved to fair-weather standard.

The total mileage proposed to be reached at the end of 1981 is 252,000 miles of surfaced roads and 405,000

* See, Vol. I, p. 75.

miles of unsurfaced roads. The Third Plan includes as cost of the road development programmes a sum of about Rs. 324 crores of which Rs. 244 crores are in the State sector and the balance of Rs. 80 crores are in the Central sector. The planned development since 1950-51 is indicated below :

Roads : Surfaced, including National Highways

(000 miles)

1950-51	97·5
1955-56	122 0
1960-61	144·0 (provisional)
1965-66	169·0 (target)

The above growth indicates a 48% increase in 1960-61 over 1950-51, and, an estimated increase of 17% in 1965-66 over 1960-61. It would seem that the expansion provided would hardly be adequate for the enormous expansion of internal trade envisaged in the Third Plan. Further, it has been pointed out earlier that wide regional disparities in the matter of road-availability is a source of weakness for the economy as a whole and that in assessing the significance of the availability of road facilities one must take into account such factors as the area, the population, the state of present development of the region concerned, the type of production (i.e. agricultural or industrial) that is required to be marketed, the plans for location of new industrial units and the expansion in the State Income expected.* It is, therefore, not enough merely to take consolation in the estimate that at the end of the Third Five Year Plan India would have 52 miles of roads per 100 Sq. miles of area as against about 30 miles at the end of the Second Plan, for in its effect on trade and commerce, it is not the All-India average growth which is important but the growth in each State as compared to its requirements.

6·4 *Regional Disparities in Road Facility.* An integrated and rapid economic development requires a well-knit road system with adequate road mileage in each State. A high national average is an illusory index of strength in the matter of road mileage for adequacy must be in relation to needs in each area, primarily in terms of total geographical area and secondarily in terms of volume of trade and commerce generated. The table given on next page indicates the inter-state disparity in regard to road development :—

* See Vol. I, pp. 124–125

State	Area in Sq. Km.		Length of National Highway in Km.		Length of State Roads in Km. Metalled		Kachcha	
(1)	(2)		(3)		(4)		(5)	
1. Andhra Pradesh	274,674	(5)	2,173	(4)	25,471	(4)	21,746	(10)
2. Assam	219,888	(7)	1,163	(10)	1,689	(13)	25,450	(7)
3. Bihar	174,043	(9)	1,321	(7)	10,295	(8)	54,666	(2)
4. Bombay	494,788	(1)	3,474	(1)	30,876	(1)	35,331	(4)
5. Jammu & Kashmir	228,802	(6)	544	(13)	961	(14)	7,187	(14)
6. Kerala	38,858	(14)	404	(14)	8,669	(10)	9,563	(13)
7. Madhya Pradesh	443,434	(2)	2,216	(3)	17,853	(6)	18,546	(11)
8. Madras	129,842	(11)	1,659	(5)	26,775	(2)	17,561	(12)
9. Mysore	191,976	(8)	858	(11)	25,978	(3)	31,163	(6)
10. Orissa	155,819	(10)	1,369	(6)	5,740	(12)	22,664	(9)
11. Punjab	121,974	(12)	1,225	(8)	7,908	(11)	22,808	(8)
12. Rajasthan	342,268	(3)	697	(12)	12,269	(7)	33,824	(5)
13. Uttar Pradesh	293,840	(4)	2,250	(2)	18,453	(5)	67,218	(1)
14. West Bengal	87.873	(13)	1,196	(9)	9,266	(9)	35,356	(3)

Source: Column (2) Surveyor-General of India Columns (3) to (5) Maharashtra State Transport Review 1961 Annual, p. 31.

N. B. 1. Figures as on 31. 3. 1959.
2. Figures in brackets indicate ranking.

It is apparent from the table given above that the extent of road development bears no relationship whatever to the basic need of a State as expressed in its total area. If, in addition, population* of the State is taken into account the results would appear to indicate a more paradoxical situation.

6·5 *Mechanised Road Transport*. The importance of road transport as a serious rival to be railways started with the emergence of motor transport, which assumed an importance in the economy of the country only after the imports of commercial vehicles, i.e. buses and trucks became fairly large. This did not happen till about 1921, and, even then the growth of the road haulage fleet was rather moderate till 1940. The real expansion took place after the Second World War, and, the decade 1950-51 to 1960-61 marked the firm establishment of mechanised road transport as a commercial factor in India. It has been estimated that during this

* See Table No. 23 in para 25·1, Ch. I, Vol I.

period the number of goods vehicles more than doubled while that of buses increased by nearly 70% for the whole of India. The State-wise growth in terms of population has not naturally been unifrom, as public vehicles, being mostly in the private sector, followed the inexorable economic law of concentrating in areas of high profitability.* Some idea, however, of the growth of motor vehicles in India can be got from the following table, though the effective growth is greater due to increase in the size and laden capacity of these vehicles :

Year	Public Service Vehicles		Goods Vehicles
	Motor Cabs	Others	
(1)	(2)	(3)	(4)
1951-52	12,264	34,637	84,013
1955-56	15,318	46,461	119,097
1956-57	16,027	38,415	126,386
1957-58	15,046	42,008	136,460

Source : C. S. O.

N. B. For State-wise details see table No. 221 C.S.O.—Statistical Abstract, 1960.

6·6 *The Economies of Road Transport.* In 1959, the Government of India set up, under the chairmanship of Shri M. R. Masani, the Road Transport Reorganisation Committee. The report of this Committee constitutes the most important detailed study of the road transport industry in India. It is interesting to note that, contrary to common prejudices, the committee did not go all out to condemn the small operator. They recommended that while formation of efficient enterprise should be encouraged in all reasonable ways, no ban should be placed on the owner of a single truck in the case of goods transport. The committee broke new ground by their assertion that "road transport works out to be more in the national interest than rail transport." The main advantages that can be claimed for road transport are :

(i) flexibility, particularly door to door service,

(ii) speed and certainty of delivery, especially for perishable commodities,

(iii) development of a personal service relation between the haulier and the consumer,

(iv) more labour intensive and offers a good scope for employment potential,

(v) caters to the needs of the interior and under-developed regions,

* See table No, 24 in para 25·1, Ch. I, Vol, I.

(vi) Economical to build and offers a stimulus to the growth of independent enterprise.

The experience of modern countries shows that economic development leads invariably to a relatively faster growth of road transport. In fact, the principle of free choice of the consumer has generally led to the share of railways in the total growing traffic declining, while that of road transport going up. In India, it is obvious that with the expansion of indigenous production of goods vehicles, there will be much greater opportunities for the transport of goods by road. In any case, as long as there is a shortage of transport generally a more rapid expansiou of road transport seems inescapable; and, in an expanding economy, perhaps, not undesirable provided infructuous investment and unhealthy competition can be avoided.

6·7 *The Future of Road Transport*. The following quotation from a press note[86] released by the Chairman of the Committee on Transport Policy and Co-ordination throws interesting light :

> "The Committee is seized of the main problem of development of road transport in the country. The history of economic development of the advanced countries of the world like U. K. and U. S. A. bears evidence to the fact that while industrial development in the earlier periods was associated with the developments of railways, road transport has been an important and potent factor in the later phases of development. With economic development and progressively growing demands on transport, road transport must play an increasingly important part in India. There are vital questions relating to development of road transport which require examination, for example, the effect of fiscal policies on development of road transport and the relationship between contributions from road transport and expenditure on roads, balancing of investment in roads and investment in vehicles etc. The road transport industry in the private sector, particularly the section of the industry engaged in freight service, is owned at present by a large number of small operators, a majority of whom just own one vehicle each. It needs to be considered along what lines reorganisation of the road transport industry is to be contemplated, so that the industry might

86. See Motor Transport, April 1962; also refer to the newspaper reports on the Press Conference held on 14th April, 1962.

be definitely expected to carry a proportion of the traffic relating to specific projects and specific regions in the country as part of the five year plans, and at a reasonable cost.

In considering the reorganisation of the road transport industry, an important factor which has to be taken into account is that the Third Five Year Plan has accepted the possibility of the extension of the public sector in the field of transport of goods by road, the principle of nationalisation having already been accepted and gradually enforced in respect of transport of passengers. Earlier, however, an assurance had been given by Government in Parliament that there would be a moratorium on nationalisation of goods transport till the end of the Third Five Year Plan, and this fact had been kept in view when the Preliminary Report of the Committee was prepared. In its final report, the Committee will have to take note of the change in the policy of Government in this regard."

An important issue has been raised in the above statement *viz* nationalisation of road transport. It is generally recognised that possible nationalisation within a short period (especially, if the period is shorter than the life of the capital asset) tends to discourage the growth of private investment in the sector concerned, and that such assets as are already in existence would tend to be used for a high rate of return which may sometimes lead to unhealthy practices and involve exploitation of the consumer. It does not, however, appear that there has been any positive adverse effect so far as investment in road transport is concerned for all new vehicles have been promptly marketed and there has been a fairly high market-value realised for old vehicles.* In short, the overall shortage of transport and the fairly high returns obtained by truck-owners has, so far at least, prevented the 'fear' of nationalisation from having any adverse effect on the development of road transport.

6·8. *The State and Road Transport.* In 1944, the Central Committee on Post-war Reconstruction recommended that public transport should be nationalised, *i. e.*, it should be State-owned and State-managed. The State Governments have been following a policy of taking over passenger services

* In fact, there are allegations of "black market" prices being realised for new trucks.

and running them as State enterprises.* The Road Transport Act (1948 & 1950) enabled the State Governments to establish Road Transport Corporations with capital provided by the State Governments and the Railways. So far, however, the preference seems to be for departmentally operated services rather than having autonomous corporations. The policy seems to be otherwise, for the Planning Commission has advised the State Governments

> "...to set up corporations under the Road Transport Act, 1950, to manage the nationalised road transport undertakings in which the railways, and, if possible, the private operators should participate."[87]

The principal reasons underlying this policy may be stated to be ;

(i) prevention of unfettered competition as between nationalised road transport and the railways,

(ii) greater flexibility of the corporation form of management,

(iii) avoidance of overlapping of State economic policy and transport policy,

(iv) more commercial and business like management,

(v) greater publicity of accounts and management decisions,

(vi) direct association of the private sector in management of nationalised undertaking.

It is unfortunate that no authoritative examination of the comparative efficiency of corporations *vis-a-vis* departmental undertakings have been made, but on *a priori* grounds one would be inclined to believe that since a corporation would not be able to get the unlimited backing of State finances as a departmental undertaking obviously could, the former should have a more commercial outlook than the latter. In any case, whatever may be the predominant future form of the nationalised road transport undertakings, it is expected that about 7500 additional vehicles will be added to the fleets of the nationalised undertakings during the Third Plan and for which a provisional estimate of Rs. 26 crores as cost has been made. In view of the large expansion of the total passenger services by road that is likely to take place, the share of the nationalised undertakings will remain unchanged at the present all-India average level of 30 per cent†. In short, the pace of nationalisation is not expected

*For Statewise details, see Vol I, p. 45

87 Third Five Year Plan, p 554

†See Vol I, pp. 40—45

to be faster than the growth of total road transport passenger services.

7. Shipping with Special reference to Coastal Shipping.

7·1 *Evolution of Shipping Policy.* The difficulties created by the Second World War led for the first time to a recognition of the inadequacy of Indian Shipping and brought about a somewhat reluctant admission that "for a country of its size, the length of its coastline and its strategic position athwart one of the world's main sea routes, India possesses a distressingly small number of deep-sea ships." The rea.isation of India's vulnerability, specially because of non-availability of adequate coastal shipping which for a country with India's coast-line must provide a natural alternative cheap transport facility, led in 1945 to the appointment of a Shipping Policy Committee. The report of this Committee, which fortunately came in 1947 and coincided with the emergence of the country's independence, may be regarded as the beginning of a national shipping policy which was incorporated formally in the Government of India Resolution of 12th July, 1947. The new policy

- (i) recognised the concept of Indian Shipping as consisting of shipping owned, controlled and managed by Indian nationals,
- (ii) postulated State financial help, assitance and encouragement for the development of Indian shipping,
- (iii) envisaged a target of at least 2 million tons *g. r. t.* of shipping within 7 years,
- (iv) aimed at 100 percent of purely coastal trade being handled by Indian Shipping, and,
- (v) hoped to increase continuously, the share of Indian shipping in India's foreign trade.

The reservation of the coastal trade of India to Indian Shipping was announced by the Government of India in August 1950. This policy of reservation was a logical necessity and provided a basic stimulus to the growth of Indian Shipping. The policy of reservation was, however, not extended to the refined products on the coast of India of the newly established refineries in 1951. Later, from 1956, tankers of Indian Shipping Companies have been engaged in the coastal movement of the products of the refineries, though till now the carriage of refined products on the coast has not yet come within the policy of reservation. The adoption of a planned economy for rapid economic development inevitably

brought shipping, like all other activities of importance, into the plan-fold.

7·2 *Shipping and Planned Economy.* With the advent of planned economy, the Goverment of India extended assistance in the form of loans to Indian shipowners for the acquisition as well as construction of ships for the coastal and the overseas trades of India. Further, facilities were given, subject to the principle of avoidance of flag discrimination, to Indian ships for the carriage of Government cargo. Finally, it was clarified that it was not Government's intention that shipping in the public sector should run in competition on routes on which existing private shipping companies have established themselves. All this had the effect of promoting shipping, and the results during the past together with the prospects during the third plan period are indicated below :

Item	1950-51	1955-56	1960-61	Target for 1965-66	Percentage increase of (4) over (2)	Percentage increase of (5) over (4)
(1)	(2)	(3)	(4)	(5)	(6)	(7)
1. Shipping	3·9	4·8	9·0	10·9	130	21
2. Major Ports (handling capacity)	20	25	37	49	85	32

Source : Planning Commission.

N.B. Shipping figures in lakh G.R.T. Port handling capacity figures in million tons.

At present, Indian ships are estimated to carry about 9% of India's overseas trade. The following figures indicate the tonnage position for the coastal and the overseas trade :

Shipping Tonnage (lakh G.R.T.)

Trade	1950-51	1955-56	1960-61
(1)	(2)	(3)	(4)
Coastal	2·17	2·40	2·92
Overseas	1·74	2·40	6·13
(Total)	3·91	4·80	9·05

Source : Planning Commission.

It will be seen that paradoxically enough the growth of coastal shipping has been slower than that for overseas trade. In fact, the targets for these two by the end of the Second

Five Year Plan were 4·1 and 4·9 lakh G.R.T. respectively. While there has been a deplorable shortfall in the case of coastal shipping, the target for overseas tonnage has been exceeded.

7·3 *Shipping in the Third Plan.* During the Third Plàn period, it is expected that about 57 ships with a tonnage of 375,000 G.R.T. will be acquired. The net addition to the existing tonnage will, however, be only 181,000 G.R.T. as about 194,000 G.R.T. would be required for replacement of overaged ships. A provision of Rs. 55 crores has been made and an additional sum of Rs. 4 crores would be available from the Shipping Development Fund which was established during the Second Plan period as a non-lapsing fund for grant of loans to shipping companies for the acquisition of tonnage. The Third Five Year Plan recognises the necessity of giving high priority to the expansion of shipping because of the saving in foreign exchange that can be effected in the expenditure at present incurred on the shipment of our overseas trade. The country would undoubtedly have liked a much higher target, but as the Third Five Year Plan[88] points out :

> "The development programme for shipping depends largely on the availability of foreign aid for this purpose, and of necessity has to be modest."

The following table gives the shipping tonnage to be acquired in the Third Plan :

Item	Private Sector	Public Sector	(GRT) Total
(1)	(2)	(3)	(4)
1. Coastal			
(i) Replacement	1,00,000	...	1,00,000
(ii) Addition	25,000	7500	32,500
(iii) Total	1,25,000	7500	1,32,500
2. Overseas			
(i) Replacement	56,000	37,600	93,600
(ii) Addition	35,200	1,13,200	1,48,400
(iii) Total	91,200	1,50,800	2,42,000
3. Grand Total (1)+(2)	2,16,200	1,58,300	3,74,500

Source : Planning Commission.

88. p. 558.

7·4 *Indian Shipping and share of Overseas Trade.* One of the basic aims of the Shipping Policy announced in 1947 was to increase the proportion of India's overseas trade carried in Indian ships. In a sense, the percentage of international trade carried is a more significant indictor of progress than figures in regard to the expansion of Indian tonnage, A progressive increase in the quantity of India's overseas cargo carried in Indian ships should follow more or less automatically in a period of continuously rising imports and exports on Government account, especially when saving of foreign exchange is a primary consideration. It must, however, be regretfully admitted that the progress in this respect has been far from satisfactory. The original target of 50% laid down in the Shipping Policy of 1947 to be achieved by 1954 was lowered to only 15% to be realised by 1961, but even this has not been achieved as a maximum of only about 9% of India's overseas trade was carried in Indian ships in the best years. The table given below illustrates the position over the years :—

Item	1951-52	1955-56	1956-57	1957-58	1958-59	1959-60
Foreign Trade						
1. Tonnage entered:						
(a) Indian	645	726	858	919	976	1207
(b) Foreign	8860	9055	9065	10,950	11,474	11,573
Total	9,505	9,781	9,923	11,869	12,450	12,780
2. Tonnage Cleared:						
(a) Indian	801	842	736	771	1,016	1,181
(b) Foreign	6,798	7,869	7,469	8,104	9,322	9,387
Total	7,599	8,711	8,205	8,875	10,338	10,568

Source : C.S.O.

The relatively slow growth of the share of Indian Shipping in a period of a nationally sponsored shipping policy together with severe restrictions on imports on private account should cause serious concern as it is very important that we should have a real awareness of the importance of shipping to our developing economy and build up rapidly a balanced merchant navy for India.

7·5 *Coastal Shipping in India.* India has a vast coastline of over 4,000 miles. Our geographical position and our economic leadership amongst the under-developed countries provides increasing prospects of trade and passenger traffic with adjacent countries. Coastal shipping has, there-

fore, assumed an added importance and now forms an integral part of our transport system, particularly as overall transport shortage in the country has recently compelled a state-sponsored policy of diverting some of the coal traffic, generally believed to be the primary responsibility of the railways, by the sea-route. The coastal shipping of India would have to become in course of time an important alternative form of transport providing not only a normal link for particular kinds of traffic specially suitable to it but also an emergent standby to be brought to the rescue of the country if, and when, any of the leading transport systems of the country fail to meet the demand. Apart from the purely economic function of providing a 'cushion', development of coastal shipping may even be important from wider considerations of non-economic necessities.

7·6 *Development of Coastal Shipping under the Plans.* The Rail-Sea Co-ordination Committee appointed by the Government of India in 1955 came to the conclusion, on the basis of cargo availability and tonnage requirements, that it should be possible to reach by the end of 1960-61 a target of 4·12 lakh G.R.T. The position and development is illustrated in the table given below :

First Plan		(Lakh G.R.T.)
On 1st April 1951	......	2·17
Target in First Plan	......	3·20
On 31st March 1956	......	2 40
Short-fall	......	—0·80
Second Plan		
On 1st April 1956	......	2·40
Target in Second Plan	......	4·12
On 31st March 1961	......	2·68
Short-fall	......	—1·44

It is unfortunate that is has not been possible to achieve the targets set, especially as the overall shortage of transport and its growing demand in a developing economy should have led normal business incentive to undertake anticipatory investments of capital in this sphere of transport activity. The Third Five Year Plan[89] proposes to add to the coastal tonnage 32,500 G.R.T. of which 25,000 G.R.T. will consist of small coastal ships for general cargo service and the remaining 7500 G.R.T. in the form of a coastal tanker.

7·7 Since the major part of coastal shipping is in the private sector*, the economic employment of the coastal fleet is essential for its development. Further, it is necessary

89. p. 558.

* Over 95% of the coastal traffic is reported to be catered by 13 Units.

to recognise that in this sector of transport the value of investment is high and the life of the asset fairly long. This means that returns must be adequate and have some assurance of permanence, at least sufficient to recover the investment made, i.e., there must be economic employment to provide the necessary incentive for the future development of shipping. In view of the peculiarities of investment in coastal shipping and in view of its significance, economic and non-economic, for the development of the country as a whole, it may not be contrary to public policy to assist its development by demarcating for it adequate traffic at economic rates. It has been the experience of other countries that bulk cargo like Coal, Salt, Foodgrains, Jutegoods, Refinery products, etc., are excellent items for coastal traffic and for India adequate cargo to keep the tonnage fully employed should not be difficult to find.

8. The State in relation to Transport in India.

8·1 Transport has always been a matter of deep concern to the Government of India—in the past for ensuring the profitability of the Indian Railways, in the present because of the conflicting interests of the different modes of transport in a background of overall general shortage. A developing economy involves an all round expansion of economic activity in which the aggregate demand on transport increases at a rate faster than the increase in the volume of gross national product. Quite apart from the requirements of planning, few governments have found it possible to leave transport—whether regarded as an industry or as a mere service—to itself, and, even the most ardent advocates of *laissez-faire* economy have tacitly regarded transport as an exception to the general rule of non-interference.

8·2 In view of the significance of transport as a factor in economic development and national integration, few in India would be inclined to treat transport merely as a commercial activity. There is a strong feeling that transport should be treated as a "Social overhead" and individual forms of transport not left to depend entirely on the maxim of self-support, which in a competitive economy would be a matter of the operation of the inexorable laws of supply and demand. A planned economy, however, cannot leave an important field of activity like transport to be determined by price-mechanism, but has to determine, against the background of a long-term policy,

> "... the role of the various means of transport" ...and a "suitable mechanism for the co-ordination of the varions means of transport."[90]

There may be good justification for holding that not only should transport costs be kept as low as possible, but that its existence is essential to economic life, and, therefore, it must even be "compelled" to exist though it may be commercially uneconomic. Such a view, if extended to particular modes of transport in specified regions for defined periods, may not be uneconomic from a national point of view; though, even when acceptable from the angle of a general principle, differences of opinion could, and would, exist as to the means of subsidisation of uneconomic trans port services. It is not easy to define the source from which such subsidy should be financed *viz.*, whether from general revenues, or from a cess on the particular commodity the transport cost of which is being subsidised or from an extra charge on all other alternative forms of transport. The difficulties in this respect would be particularly great in a mixed economy where particular a form of transport and a part of other forms of transport are in the public sector. Broadly, however, the general view is to hold that since subsidisation must be a special case justified in the wider national interest, the national exchequer must find the resources for the granting of such subsidy and for which a decision, with adequate justification, must be taken at a national level.

8·3 It would be necessary to define the objectives which Government should appropriately have when it decides to intervene in the field of transport. It would be desirable to recognise that the considerations could be either economic or non-economic *i.e.* political or social. Where non-economic considerations lead to intervention, there obviously can be no question of evaluating costs in terms of gain, for the two would be on entirely different planes. Thus, for instance, if Government decides to intervene for reasons of national safety and requirements of military movement, obviously no costs could be prohibitive. Again, if intervention is undertaken for maintaining the stability of the social structure, as, for example, might well be argued in favour of protecting bullock carts from being annihilated by competition of mechanised transport, the calculations of cost would perhaps be superflous. Broadly, however, one may indicate the objectives with which Government may intervene in the field of transport as follows:—

(a) ensuring adequate overall development,

90 See terms of reference of the Committee on Transport Policy & Coordination, p. 1 Prelimanary Report.

(b) securing appropriate regional spread,
(c) avoiding uneconomic national investment,
(d) preventing exploitation of consumers,
(e) improving efficiency, including lowering of costs, greater safety and planned regularity,
(f) providing for a "cushion" to carry seasonal excesses, and, take care of unestimated economic growth.

Experience of economic development in other countries reveals that with rising prosperity comes the opening of new areas, growing urbanisation and a general extension of markets. All these factors, together with widespread regional development, often brings about a more than estimated volume of traffic. Transport planning, therefore, inevitably implies the recognition of a necessary excess provision at all stages so that the supply of transport keeps ahead of its demand. In a planned economy, the requirements of transport facilities should be estimated well ahead of their actual necessity and steps taken in anticipation to develop necessary capacity for transport, perhaps more than any-other activity, requires a longtime to fully develop. At the same time one must bear in mind that after a certain stage of development is reached, the pace of expansion of freight traffic tends to slow down so that as has been rightly pointed out:—

> "It is much better to direct investment in right channels with a clear-cut conception of our objectives and policies than to seek remedial measures after infructuous investemnt has been made."[91]

91 Committee on Transport Policy & Co-ordination, Preliminary Report, p. 126.

VIII

FOREIGN TRADE AND FISCAL POLICY

1. Nature and Importance of Foreign Trade.

1·1 The old concept of International Trade was a concept of multilateral exchange amongst many countries with the benefits of the principle of comparative costs realised by all participants in some degree or other, even though extremely unfavourable terms of trade for particular countries was not unknown. In fact, since climate and natural resources must vary from country to country, and, acquired skill and level of industrial development differ, the concept of economic inter-dependence of nations is a logical one for promoting world prosperity. While one would not be inclined to accept the extreme proposition that a decline in international trade is a sign of deliberate or imposed impoverishment, one must also avoid the fallacy of confusing self-sufficiency with the economic desiderata of providing fuller employment and higher living standards.*

1·2 Whatever may be the theory of the advantages of foreign trade, the fact remains that the Second World War left a legacy of restrictionism in trade and the goal of a relatively free multilateral trade seems a dream. Foreign trade to-day has acquired a somewhat inflexible form and a growing tendency towards tariff barriers, import controls, foreign exchange regulations and bilateralism or regional trade blocs have all contributed to this inflexibility. Of course, it has often been argued that these trends are inevitable in the short period context of planned development and that in the long period global multilateral trade on a freer basis is the aim; one is, however, tempted to recall Keynes' cynical axiom that "in the long period we are all dead."

1·3 To India, planned development perforce restricts multilateral trade. Being an under-developed country India must import to aid development, this in turn must necessarily

*See Vol. I, pp, 223-224.

lead to an intensification of trade relations with those countries imports from whom imply greater investment to finance her development programmes. Since trade deficits and overall balance of payments deficits must lead to a drive for stepping up exports, there is an unavoidable reliance on State trading and bilateral trade agreements. It would seem that this paradoxical trend in our trade policy must perforce continue till the "take-off stage" is reached and economic development attains self-sustaining growth.[92]

1·4 It is often loosely believed that an increase in a country's international trade is a sign that it is availing itself of its opportunities to raise its standard of living through the mechanism of exchange. There is sometimes an unfortunate tendency to identify the quantum of a country's foreign trade as a sign of prosperity. More subtle and pseudo-learned arguments link a country's foreign trade with its national income or its population as indicators of prosperity. Such reasonings are fallacious. Neither the percentage ratio of the foreign trade of a country to its national income nor its per capita foreign trade are good (or even satisfactory) indicators of the high or low stage of development of that country. In fact, a highly developed economy with a substantial national income should normally be expected to have its higher rate of progress sustained by internal demand and, therefore, its foreign trade is likely to be a small proportion of its national income. On the other hand smaller and more compact economic systems may find the home market unable to provide a sufficient basis for a sustained productive effort and may seek to earn a greater share of its national income from its foreign trade. In fact, no clear relationship can be established between national income and foreign trade as the table given below would reveal:

(In Million U.S. Dollars)

Country	National Income	Total Foreign Trade (Import+Export)	Percentage of (3) to (2)
(1)	(2)	(3)	(4)
India	26,418	3,172	12.0
Australia	12,024	3,862	32.1
Canada	26,234	11,111	42.4
Ceylon	1,128	789	69·6
U K.	53,007	20,131	38.0
U.S.A.	399,600	32,443	8.1
West Germany	44,887	18,283	40.7

N. B. Figures relate to 1959.

92 See Problems in the Third Plan, article by Dr. I.G. Patel on "A Self Generating Economy."

Even allowing for limitations of international comparisons it is obvious that column (4) hardly gives any proper index to the country's basic economic prosperity for it would perhaps be absurd to conclude [as the figures in column (4) tend to indicate] that India is more prosperous economically than U.S.A. or that U.K. is less developed than Ceylon or Canada. So far as per capita foreign trade figures are concerned, apart from the difficulty of computing comparable figures due to non-availability of a common-year census estimate of population, the concept itself is hardly worth examination for the *size* of a country's population has little significance for its stage of economic development or its foreign trade.

2. Trends in India's Foreign Trade.

2·1 The immediate post-Independence years were years of uncertainty and difficulty for the country's foreign trade. The partition led to deficits in food, raw cotton and raw jute. The devaluation of the rupee in September 1949 and the Korean war boom helped to restore our foreign trade, but these advantages were short lived. The inauguration of planning, which unfortunately coincided with a deterioration of our food position, led to a rapid rise of imports resulting in increased adverse balances of trade. The success of our food production programmes helped to reduce our food imports*. The need, however, of increased imports of machinery, industrial project equipment, industrial raw materials etc. needed for the country's planned development continued to strain our balance of trade position, in spite of a rigorous import control policy and vigorous attempts at export promotion. The balance of trade position has during the first two plan periods been rather unsatisfactory, and in the context of India's adverse position on capital account, was a basic source of worry to the country. The table given below indicates the trends of our foreign trade.

(Value in Rs. Crores)

Item	1951-52	1956-57	1958	1959	1960
(1)	(2)	(3)	(4)	(5)	(6)
I. Merchandise.					
(a) Imports	979	903	878	940	10,17
(b) Exports	729	614	572	614	629
(c) Re-exports of (a)	14	6	10	7	12

* See Vol. I, Ch. V.

(1)	(2)	(3)	(4)	(5)	(6)
II. *Treasure*					
(a) Imports	45	30	1	1	1
(b) Exports + Re-exports	2	4	—	—	—
III. *Balance of Trade*					
(a) Merchandise	–236	–283	–296	–320	–376
(b) Treasure	–1	=	–1	–1	–1
(c) Total (a)+(b)	–237	–283	–297	–321	–377

Source : C. S. O.

N. B. The sudden changeover in 1957 to calender year in place of the usual financial year is one of those "improvements" which worry the unfortunate user.

The above table reveals the following trends :

(i) imports have risen substantially during the Second Plan period, the decline in 1958 being rather isolated and temporary ;

(ii) exports declined substantially in the first two years of the Second Plan period, and then started reviving, though the figure of 1960 is still substantially lower than that for 1951-52 ;

(iii) the adverse balance of trade in merchandise has been steadily on the increase, the Second Plan period showing a steep rise.

The increase in the imports is obviously a reflection of the tempo of our economic and industrial development as the major portion of these were machinery, base metals and metal manufactures, which taken together increased from 20% of total imports in 1951-52 to nearly 40% in 1959-60; on the other hand, substantial decline took place in the imports of raw cotton and raw jute. The composition of the exports also underwent substantial changes with those of raw materials declining sharply. The country is now an exporter in a substantial way of engineering and electrical goods, diesel engines, sewing machines, electric fans etc. in addition to large exports of the traditional items like cotton piece goods, jute manufactures, tea, tobacco, manganese, mica etc.

2·2 *Foreign Trade under the Plans.* The country has so far gone through a decade of planning and, not surprisingly, planned economic development has exercised an important

influence on its foreign trade. The guiding principles of India's commercial policy, as laid down in the context of planning are :

(i) It must assist in achieving the production targets in the Plan,

(ii) quantum and value of exports should reach increasingly higher levels,

(iii) the composition of imports and exports must further the implementation of the Plans,

(iv) the deficit in the balance of payments must, as far as possible, not deplete the foreign exchange resources at the disposal of the country, and

(v) trade relations must maintain a fair degree of continuity with given countries.

As is to be expected, the plans led to a stepping up of the total foreign trade of the country, imports increasing substantially but both imports and exports undergoing important changes in composition and direction. The significant change that has come about would be clear from the following table :

Imports 1951-61

(Rs. Crores)

Category	1951-56 (annual average)	1956-61 (annual average)
1. Consumer goods	235	247
2. Raw materials & Intermediate goods	364	502
3. Capital goods	125	323
Total	724	1072

Source—Planning Commission.

It will be seen that there has been only a small—almost insignificant—rise in imports of consumer goods, while the rise in capital goods was by more than 150%, and that of raw materials and intermediates (the imports of which are indicators of rising manufactured production within the country) was by about 50%. Exports, on the other hand, were fairly stagnant during the last decade—the first plan annual average being Rs. 609 crores as against Rs. 614 crores of the Second Plan. The comparative stagnation of exports is a natural corollary of economic development which must immediately increase (because of an increase in aggregate

incomes) domestic demand, thereby reducing availability of surplus for exports. Further, in the early days of industrialization, comparative costs generally remain to the country's disadvantage, preventing any rapid expansion of exports immediately. However, though the quantum of exports did not (in fact, could not be expected to) increase rapidly or substantially, its pattern underwent a change reflecting the changed structure of production emerging in the country. It must, of course, be recognised that the changed pattern of exports was partly also forcibly brought about by the change in the economy resulting from the partition. On the whole two trends in our exports are perceptibly noticeable, *viz.*

(a) emergence of a wide range of engineering, electrical and other manufactured goods—particularly of industries introduced since the attainment of Independence, and

(b) growth of exports of processed goods rather than raw materials.

These changes, however, did not reduce the significance (in spite of decline in their quantity) of the exports of commodities directly or largely based on agricultural production such as tea, cotton textiles, jute manufactures, hides and skins, tobacco etc, and these continued to account for the bulk of the country's exports.

Pattern of Exports 1951—61

(Rs. crores)

Category	1950-51	1955-56	1958-59	1959-60
(1)	(2)	(3)	(4)	(5)
1. Agricultural commodities & related manufuctures of which	496·5	489·3	453·5	473·6
Cotton & Jute manufactures	250·5	181·7	153·4	180·5
2. New manufactured products	8·9	8 6	12·5	25·0
3. Other manufactures	49·5	52·4	40 8	80·0
4. Minerals	23·4	34·4	46·2	53·0
Total	578·3	584·7	553·0	631·6

Source : Planning Commission

2·3 *Relative growth of Imports and Exports.* It has already been pointed out that during the decade 1950-60 imports increased substantially but exports were more or less stagnant. This can be forcefully brought out by constructing an index of the volume of imports and exports during the period as indicated in the table below :

Year	Index Volume of Imports	Exports
(1)	(2)	(3)
1952-53 (Base)	100	100
1953-54	93	100
1955-56	116	115
1957	156	119
1958	140	108
1959	148	119

Source : C. S. O.

N. B. 1. The sudden changeover in 1957 to calendar year in place of the usual financial year is perhaps one of those "improvements" which characterise statistics in India and which are a constant source of worry to the unfortunate user.

2. Recently a different series has been put out with 1958 as Base year = 100; see Statistical Handbook of the Indian Union, issued by the C. S. O. 1961 edition pp. 114—117.

3. Later figures not available.

It would appear from the table given above, that against a 48% growth in imports (which reached earlier a peak increase of 56%) there has been only a 19% increase in exports, leading obviously to a worsening of the trade-balance position.

2·4 *Direction of Trade.* A significant change in the quantum and composition of trade would normally be expected to also bring about a change in the country-wise distribution of our foreign trade, for obviously sources of supply and demand must, under the changed circumstances, undergo variations. The process of change in the direction of trade is further stimulated by changes in relative efficiencies of production brought about by the process of economic development at home and abroad. In recent times, however, a new factor has begun to exert a significant influence *viz.*, aid programmes and trade-agreements which canalise trade into determined channels. Broadly, the earlier historical associations have continued to exert their influence and sterling

area countries, with U.K. playing the leading role, continue to play a major part in India's foreign trade. A substantial portion of the country's exports has always found its market in the sterling area, which has also been the supplier of a sizable proportion of our imports. Heavy requirement of planned development have led India to look more and more to other industrially developed countries for assistance and cooperation, and naturally U.S.A. and the dollar areas have, in recent times, been participating increasingly in our foreign trade. The following table brings out changes in the direction of India's foreign trade during the First and Second Plan periods :

Direction of India's Foreign Trade

(Percent Share)

I Country/Area	II Exports 1952	1956	1960	III Imports 1952	1956	1960
	(a)	(b)	(c)	(a)	(b)	(c)
1. ECAFE Countries	25·7	16·3	17·0	13·6	12·4	13·1
Japan	4·1	4·9	5·5	2·4	5·2	5·4
2. West Asia	5·7	5·8	6·5	7·7	10·8	7·5
3. Africa	3·6	3·9	2·5	3·8	4·0	4·4
4. Western Europe	29·6	39·8	38·5	30·1	50·1	40·4
U.K.	20·5	29·8	27·5	18·5	25·0	20·0
European Economic Community	7·5	8·3	8·0	8·8	20·0	18·0
5. Eastern Europe and China	1·3	3·5	8·0	2·2	4·2	3·7
6. North America	21·1	17·0	18·7	37·3	12·4	25·2
U.S.A.	19·0	14·7	16·0	33·6	11·3	23·7
7. Latin America	1·4	1·0	2·5	...	0·1	0·1
8. Oceania	4·3	4·4	3·1	2·0	1·7	2·3
9. Others	7·3	8·3	3·2	3·3	4·3	3·3
	(100)	(100)	(100)	(100)	(100)	(100)

Source : Planning Commission

The trends revealed by the above table are interesting. It would appear that :

(a) concentration of both exports and imports is noticeable for Western Europe, with U.K. continuing to be the largest single country in this group.

(b) U.S.A. has emerged as the chief source of our imports, though her share in 1960 is lower than what it was in 1952.

(c) the decade of planned development has led to a narrowing of the field of our exports, the largest single share being that of U.K. but its percentage share going up from 20·5 to 27·5; but a wider diversification of imports is noticeable in the sense that the predominance of U.S.A has declined.

(d) the share of U.S.S.R. and countries in Eastern Europe has increased substantially in regard to exports and significantly for imports.

3. Balance of Payments[93]

3.1 *The Concept.* Trade in goods across national frontiers gives rise to claims for or against a country. It is this wider concept of the sum of debts due to a country and that of debts due by it that constitutes what may be called the equation of indebtedness or the balance of payments. In the accounting sense it implies a systematic record of all economic transactions[94] between the residents of a given country and residents of other countries. Balance of Payments of a country is the final result (debit or credit) during a given period of time on account of

(i) merchandise trade, including bullion, in the form of exports and imports,

(ii) payments due for transactions relating to services, and

(iii) borrowing and lending operations—both on private account or government account.

Items (i) and (ii) create little conceptual difficulties, and, normally the balance of trade is said to be "favourable" if export-earnings exceed import-payment liabitities, including in the former earnings due for services (e.g., shipping, banking, insurance, etc.) rendered and setting off against the latter debts due for services secured. The concept of capital movements included in (iii) is, however, a little more complicated as the time-factor is significant. A borrowing nation becomes a creditor in the short period while the

93. See Bastable International Trade, Ch 14.

94. See Haberlar Theory of International Trade, Ch. II.

proceeds of the loan are being moved into the country, though once the loan operation is carried out, the lending country necessarily becomes the creditor for purposes of receiving interest payment and capital repayment. In view of the enormous volumes of international borrowing and lending, especially aid-transactions* connected with programmes of economic development in under-developed countries, the concept of the balance of payments has become one of supreme significance, especially as any deficit in it can be met only either by external assistance or by a draft on foreign exchange reserves.

3·2 *The Trends.* It is interesting to study India's Balance of Payments during the Plans as indicated in the table given below:

(Rs. crores)

Item	First Plan (1951-56) (Actuals)	Second Plan (1956-61) (Revised Estimates)	Third Plan (1961-66 (Estimate)
(1)	(2)	(3)	(4)
1. Imports (c.i.f.)	3632·9	5374·5	6350
(a) private	2714·2	3111·2	
(b) government	918·7	2263·5	
2. Exports (f.o.b.)	3108·5	3060·8	3700
3. Trade balance (2—1)	—524·4	—2313·7	—2650
4. Official donations	95·9	191·8	...
5. Other invisibles (net)	391·8	428·5	...
6. Current account (net)	—36·7	—1687·5	—2650
7. Errors and omissions	—97·5	—47·2	...
8: Official loans (gross)	106 6	790·0	3200
9. I.M.F. Drawings (net)	—41·5	54·7	
10. Other Capital transactions (net)	—52·2	291·2	—550
11. Draft on foreign exchange reserve	121·3	598 8	...

* See Vol. I, Ch. XII.

It will be seen that the position was not unsatisfactory during the First Plan. This was partly because the First Five Year Plan was directed mainly towards increasing agricultural production and strengthening the economic overheads of development, like irrigation, power and transport. So far as industries were concerned, more emphasis was laid on utilisation of existing capacity more fully. All this implied that the direct requirements of foreign exchange in the First Plan were small. The position was, however, radically different in the Second Plan. The direct foreign exchange requirements of the planned investment was substantially larger. Further, increasing demands for imports were felt due to the growing needs of a developing economy. In addition, two bad agricultural seasons led to large food imports. The net result has been a serious drain on our foreign exchange reserves leading to the necessity of a stringent import control policy and a vigorous export-promotion programme. The position as estimated for the Third Plan is also not particularly comfortable and the problem of the external resources* for the Third Plan continues to be an important worry, especially as the aggregate reserves (excluding gold but including government balances) at the beginning of the third plan amounted to only Rs. 186 crores as against Rs. 785 crores at the beginning of the second plan. The Third Five Year Plan[95] has frankly recognised the seriousness of the position and has categorically stated :

> "It has been evident for sometime past that a greatly intensified export effort is essential if the country is to be in a position to meet its growing import requirements and to move forward progressively towards a balance in external accounts. The objective...... is to ensure that the economy is able to earn enough by way of exports so that it can, after a period of ten years or so reduce substantially the dependence on assistance from abroad. Considerable stress has been laid on export promotion for the last two or three years. What is needed now is a clear acceptance of the sacrifices involved and sustained follow-up action with a view to getting results on a scale that is commensurate with needs."

3·3 *The problem.* It is necessary to emphasise that, unfortunately, the overall balance of payments has continued to remain difficult in the first year of the third plan ; and in view

* For a general discussion of the resources for the Third Plan, see Vol, I, Ch. XI, para 4.

95. p. 111.

of the low level of reserves from which the plan started it became necessary to draw on our second line of reserves with the International Monetary Fund. In fact, the enormous drain on our Foreign Exchange Reserves is a point worth noting carefully, and the position is indicated below :

India's Foreign Exchange Reserves

(Lakhs of Rupees)

End of	Assets (a)	Movement (Increase + Decreare—)
(1)	(2)	(3)
1950-51	951,41	+ 28,55
1955-56	824,61	+ 10,47
1956-57 (b)	681,10	—143,51
1957-58 (c)	421,22	—259,88
1958-59	378,92	— 42,30
1959-60	362,87	— 16,50
1960-61	303,61	— 59,26
Dec. 1961	316,74	+ 13,13
Jan. 1962	304,02	— 12,72
Feb. 1962	302,35	— 1,67

Source : Reserve Bank of India.

N.B. (a) include (i) 7·1 million ounces of gold held, valued at Rs.21·24 per tola till October 5, 1956 and thereafter at Rs. 62.50 per tola, vide Reserve Bank of India (Amendment) Act, 1956, Section 33,
(ii) foreign assets of Reserve Bank of India,
(iii) Government balances held abroad.

(b) include net borrowing from International Monetary Fund of Rs. 55 Crores.

(c) include the stand-by credit of Rs. 34·5 crores.

It will be seen that there has been a steady deterioration in our foreign exchange reserve—the deterioration in 1955-56 being much greater in reality if account is taken of the upward revision of the value-price of gold held in the reserve. There was a slight recovery in the first half of 1961-62, but the position deteriorated again. Strangely enough, the pressure on balance of payments in the first half of 1961-62 has persisted despite lower imports and a significant improvement in exports. It seems, therefore, that the continuation of the difficulties in balance of payments is due

to deterioration in regard to invisible transactions, both current and capital.[96]

4. Regulation of Foreign Trade.

4·1 *Import control.* The origin of import control lies as far back as May, 1940, when as a war-time measure it was introduced under the Defence of India Rules. The intention originally was a very limited one *viz.*, conserving foreign exchange and shipping space. Subsequently, with the development of planning, the scope of import control widened and to-day practically the import of all goods is controlled—the exceptions being so few as to be negligible. The objectives of import control policy have also undergone considerable changes and now it serves not merely as a means of saving foreign exchange but assists in industrial development and acts as a limited instrument of price moderation. A decade of planning has altered the situation radically. In 1950, India had large sterling balances to her credit and a sizeable 'invisible' income; to-day foreign exchange has become extremely scarce. The dawn of independence found us with a low level of industrial development, a poverty-stricken population and a State which had few obligations for promoting social and economic welfare ; 1962 finds us inaugurating the Third Five Year Plan, with ambitious tasks of social and economic reconstruction that are making heavy demands on the country's resources. The Third Plan, however, starts with depleted exchange reserves, a sizeable foreign debt, a large adverse balances of payments and practically no net 'invisible' over-sea income. The requirements of foreign exchange in the Third Plan is substantial, being nearly Rs. 5,750 crores in a total investment reckoned at Rs. 10,400 crores.[97] Under such circumstances, the import control policy has to be viewed with great caution, for its role now is to perform the twin functions of conserving foreign exchange resources and promoting the healthy functioning of an economy that aims at rapid growth and rising standards of living. The objectives of Import Control have been defined thus :

> "The policy and procedure of Import Control has to be so regulated as to be in consonance with the main objectives and the strategy of the Plan itself. Import Control must serve as an instrument of industrial development, as a conservator of foreign exchange and as a vehicle of export promotion. It

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96. For details, see Government of India's Economic Survey, 1961-62, issued with Budget Papers, paras 40-43.
97. See Third Five Year Plan, pp. 110 and 112.

> must strengthen the industrial base of the country, diversify the economic structure, and create conditions of a self-generating economy, so that the nation can go forward to the maximum extent possible on its own steam."[98]

In a sense, import control to-day is a part of planning. It is designed to influence the balance of payments position, both absolutely and in its composition by keeping out specified types of imports and substituting certain types by others. In fact, by keeping out imports of consumer goods and obtaining instead capital goods, it would be possible to develop production lines that may not only avoid the necessity for imports but may actually stimulate exports. It is a far cry from the old classical proposition of 'imports pay for exports, to a concept of curtailment of imports for promoting exports. For a proper understanding of the problem of import-control, it is necessary to distinguish between :

(i) non-essential consumption imports,
(ii) maintenance imports, and,
(iii) development imports.

So far as (i) is concerned the necessity or desirability of cutting them down in the interests of conserving of foreign exchange would hardly be questioned. It is true that their severe curtailment may lead to an unjustifiable rise in the prices of local substitutes, especially as producers in India are not averse to taking advantage of conditions of scarcity and a rising standard of living where too much money is chasing too few goods. Such price rises would have to be accepted as part of the price for planned development, and one can only hope that governmental action would tend to squeeze back for the country the proceeds of such conjunctural excess profits and incomes. The distinction between 'Maintenance' imports needed for the existing units of Industry at the optimum level of production and imports for the 'Development' of new units is important, but it would be unwise to ignore that they are two facets of the same phenomenon. It is neither possible to keep the two in watertight separate compartments nor can there be any hard and fast line of demarcation between the two. It would be obviously uneconomic to reduce maintenance imports below the level which is necessary for optimum utilisation of existing capacity, for unutilised installed capacity is a national waste; it would be equally wasteful to cut

98 Minister for Commerce and Industry ; quoted in Report of the Import and Export Policy Committee (1962), p. 7.

down development imports which bring out 'developments' which are necessary for keeping the existing industrial units in full production by stimulating the production of (a) power, (b) transport and (c) raw materials and components for the existing units. The two sectors of the economy—the existing and the new—are, in effect, interdependent, each providing a support to the other, and, in the long run, import control policy must necessarily hold a balance between the competing claims of the two for scarce foreign exchange resources. In one field, however, the two are not competitive, *viz.*, the new industries which are being developed with specific foreign aid where obviously imports are 'tied' so that there is little choice in the matter and no possibility of diversion of development imports to maintenance imports. In any case, the needs of total imports have been on the increase, and, inspite of a policy of rigid control and restrictionism, the decline in aggregate imports has not been sufficiently marked to affect significantly our balance of trade position. The history of our import-control policy can be broadly demarcated, according to basic trends, into the following broad periods :

(*a*) *1947 to June, 1948*; ...a policy of restriction and curtailment of imports, import trade control being linked closely with foreign exchange control and the balance of payments problem ;

(*b*) *1948 to June 1949*;...a policy of liberalisation of consumer and industrial goods to combat inflationary trends, as it was felt that the restrictive import policies were imposing on consumers a measure of austerity which was not warranted by the limitations of the country's foreign exchange balances, particularly with soft currency areas ;

(*c*) *1949 to June 1954*;...revival of restrictionism resulting from a fall in dollar-export earnings, which were further adversely affected by the devaluation of the pound sterling to which the rupee was linked. It was necessary during this period to make severe cuts in imports from the dollar areas ;

(*d*) *1954 to December, 1956*;......this was a period of intense liberalisation, during this period we find that not only large imports of machinery, capital goods and raw-materials were permitted to keep up the tempo of development (a feature which was perhaps an inevitable corollary of planned industrialisation) but the import of consumer goods was also substantially liberalised ;

(e) *1957 to 1962* ;—recurrence of foreign exchange difficulties led to a return to the policy of restriction and control. The early part of the period involved India having to finance her import programme practically by 'cash payments' out of her own resources because of difficulties in obtaining overseas credits and long-term loans.

It is apparent that our import-control policy has been vascillating, and was determined more by immediate and short-period considerations than by any well planned long term view. One might even maintain that it was not till the last phase that any judicious distribution of the limited foreign-exchange resources was undertaken, so that only recently has the policy been directed towards ensuring imports of commodities essentially required for a developing economy. At present, the accent is on the import of industrial raw materials, and, plant and machinery, simultaneously with severe curtailment of consumer goods. Some idea of the variations in the import-control policy can be got by analysing the trends in the policy-statements of three divergent periods, as indicated in the table given below:—

Trends of Import Policy

Period	No. of items on O. G. L.	No. of items carrying quotas of			No. of items banned
		50% & above	10% to 50%	below 50%	
(1)	(2)	(3)	(4)	(5)	(6)
July-December, 1952	153	110	17	12	200
July-December, 1956	109	215	211	91	153
Oct1960—March 1961	NIL	18	56	78	730

N.B. Approximate figures constructed from the Red book on Import control.

It would be legitimate to examine how the policy has affected the composition of our imports. This can be illustrated by the following table which brings out clearly the substitution of consumer goods by industrial goods that has taken place during the lastdecade.

Break-up of Imports

(Percentage distribution)

Type	1952-53	1955	1959	1960
(1)	(2)	(3)	(4)	(5)
1. Capital goods	12·5	15	14·4	14·3
2. Industrial goods	46·5	55	61·4	68 9
3. Consumer goods	41·0	30	24·2	16·8
	(100)	(100)	(100)	(100)

N.B. Rough approximation constructed from figures of principal items of merchandise imports.

4·2 *Export Promotion.* Policy on the export side has been one of progressive relaxation and decontrol taking into account the internal needs of the country. Considerable emphasis has been, of late, laid on a determined policy of export promotion. It has been frankly recognised[99] that

> "It has been evident for sometime past that a greatly intensified export effort is essential if the country is to be in a position to meet its growing import requirements and to move forward progressively towards a balance in external accounts. The objective...is to ensure that the economy is able to earn enough by way of exports so that it can, after a period of ten years or so, reduce substantially the dependence on assistance from abroad."

The foreign exchange crisis towards the middle of the Second Five Year Plan compelled urgent attention being paid to stimulating exports and during the last few years considerable stress has been laid on export promotion. Major steps that have been taken to stimulate exports are :

(i) decontrolling export items and placing them on the free licensing list ;

(ii) granting of railway freight rebates on specified export commodities ;

(iii) formation of Export Promotion Councils for particular commodities and Commodity Boards for important items. The function of these Councils and Boards being to

(a) provide information and assistance,
(b) undertake foreign market studies,

99. Third Five Year Plan, p. 111.

(c) conduct propaganda by sending out trade delegations,

(d) lay down standards of quality and packing,

(e) assist as arbitrators or valuers, by agreement, in the settlement of disputes and differences arising out of export transactions ;

(iv) setting up of the Export Risks Insurance Corporation (1957) to offer facilities to exporters to insure normally non-insurable risks arising in the course of export trade ;

(v) giving of drawback of Import Duty and rebate of Excise Duty so far as raw materials and components used in producing finished export goods are concerned ;

(vi) establishment of the State Trading Corporation "to organise and effect exports from and imports into India".

In addition to the above, schemes have been devised under which import licenses are granted to the exporter with reference to his export performance. The chief idea behind such measures is to enable replacement of the imported raw material content of the products exported. Sometimes, such licenses are given on a "loan basis", in anticipation of exports which subsequently become obligatory.

The Third Five Year Plan takes the total receipts from exports at Rs. 3700 crores as compared to the actual receipts of Rs. 3053 crores during the Second Plan period. The estimate of Rs. 3700 crores is the minimum to be aimed at, though the needs of the situation, in fact, demand a much higher target. It is, however, necessary to recognise that exports do not materialise merely by wishful thinking—they require competitive efficiency, and, only when export-prices of Indian goods in the world market are lower than those of our competitors would it be possible for our exports to grow. There are certain factors which should be borne in mind, for these may obstruct the realisation of the export target. We must remember that a rising standard of living must make increasing demands for home consumption and it would be idle to preach[100] that "foreign exchange earnings have at the present juncture to be increased even by sacrifice of domestic consumption," unless one were prepared to sacrifice considerably the freedom within planning which is a significant characteristic of present day economic

100. Third Five Year Plan, p. 113.

structure in India. Secondly, our internal costs of production are continuously on the rise due to general inflationery trends, rising labour charges due to a progressive labour-policy, increasing burden of indirect taxation made necessary by the needs of raising large internal resources and the high capital-cost at which our industrial units are being set up. It would be unwise to forget that in course of time countries importing our exports would themselves want to replace them with local products and that the most serious threat to our exports may come from economic development of underdeveloped countries with "untied" markets, for we could not possibly continue indefinitely to tie our imports with our exports. Thirdly, the export demand for our traditional items have hardly been very buoyant lately, and, our staple export commodities have not only to face severe fiscal and quantitative restrictions abroad but also deal with increasing competition from the rest of the world including the growth of substitutes. Thus complacency in the matter of export promotion would be suicidal, especially if such promotion continues to be based on "aids and incentives" rather than on the economics of comparative advantage. Finally, artificially stimulated exports are generally like soap-bubbles in sunlight—attractive to look at but with a tendency to burst at the most inconvenient moment. It is, therefore, dangerous to derive much comfort from the trends of export earnings in recent years.

Export earnings have, undoubtedly, shown progressive increase during the last three years and have been as follows:

Year	Export earnings (f.o.b.) (Rs. Crores)
1958-59	576·3
1959-60	623·2
1960-61	631·2
1961-62 (April—Sept.)	320·3
1961-62 (Estimated)	665·0

These figures indicate a steady increase ; but, they are, partly at least, illusory and do not represent a full quantum of improvement for some of the rise in export-earnings is the result in the main of special factors, such as exceptionally high prices of jute manufactures. From the rate of rise in export-earnings, it would seem that realisation of the target of Rs. 850 crores a year by the end of the Third Plan period would be difficult unless a great deal of further effort to promote exports are undertaken.

5. Fiscal Policy.

5·1 Development of international trade has often been treated as proof *ipso facto* of gain by national specialisation, and advocates of allowing foreign trade to develop under conditions of freedom often quote Marshall[101] to argue that

> "If goods, which can be produced at home, are yet imported freely from abroad, that shows that they can be got generally at less cost by making other things with which to buy them from abroad than by the direct method of making them at home".

This, in essence, is the doctrine of comparative advantage, whereby international specialization is treated as synonymous with world prosperity and national gain. It has, however, been increasingly recognised that the State does not exist only for economic purposes; it has a positive role to play in developing the national ambition of a country*, and, that ambition may be somewhat different from merely maximisation of a sum total of aggregate gains, especially if one recognises the possibility of conflict between the economic interests of the nation as a whole and of some of its members.

5·2 The doctrine of protectionism is based on the twin foundations of relative differences in economic development of countries and the aspirations of underdeveloped nations to acquire the power and capacity to produce in preference to the utility-value of what can be produced under conditions of freedom of trade. Schmoller stated this clearly, though some what crudely, when he asserted that :

> "The free-traders forget that unrestricted Free Trade between all countries brings about increasing sales and rising prosperity for the countries favoured by Nature and historic development but, in the case of those neglected by Nature it may easily rob them of their industries, or even in certain circumstances of a portion of their population. No people with a national consciousness can permit that without defending itself."

In the context of the almost universal urge for development in under-developed countries, the theory of protection acquires a new orientation and is to-day a weapon not merely for safeguarding the interests of particular industries but an overall asset for regulating foreign trade to promote economic development.

101. Official Papers, p 391.
* See Vol. I, pp. 1—6.

5·3 The role of protection as a means for industrial development was first propounded in the concept of 'discriminating protection' by the Fiscal Commission of 1923. Their formula required that an industry receiving protection should satisfy the three conditions :

(a) possess natural advantages in regard to raw material, power, supply of labour or a large home market,

(b) that without protection there was no likelihood of the industry developing at all, and

(c) that it had sufficient ultimate comparative efficiency as to be able to face outside competition eventually without protection.

The charms of discriminating protection held leading Indian economists in awe for almost a generation and few noticed that the rigid application of these conditions had prevented many nascent industries from receiving protection and retarded setting up of industries that might be considered key industries or of strategic importance. It is true that the powers of the *ad hoc* Tariff Boards set up in 1945 were wide and they could recommend protection to any industry if they were satisfied that it was an industry to which assistance should be granted in the national interest. Even then, the Tariff Board was required to satisfy themselves that

(i) the industry was an established one,

(ii) it was conducted on sound business lines, and,

(iii) it would be able to do without protection within a reasonable time.

It is obvious that even with the widened scope, the Tariff Boards were severely impeded in their discretion and were unable to use protectionism as part of a dynamic policy for planned development of industries. It was only with the dawn of independence that the country could visualise the development aspect of protection, and boldly assert in its resolution on Industrial Policy* that :

> "A dynamic national policy must be directed to a continuous increase in production by all possible means," and, that "the tariff policy of Government will be designed to prevent unfair foreign competition and to promote the utilisation of India's resources, without imposing unjustifiable burden on the consumer."

* See Vol. I, p. 238.

5·4 The report of the Fiscal Commission of 1949-50 marks the entry of Indian protectionist policy in its last and final phase *viz.*, linking protection of industries to an overall planning of economic development and making tariff protection an instrument for furthering economic development of India. Economic Development in India is more or less synonymous with the idea of industrialization, and tariff protection has to play the role of assisting in the development of industries.* Broadly, one could sum up the main aspects of a dynamic policy of protection as implying the following:

(a) all defence and strategic industries should be protected on national considerations, whatever the cost;

(b) protection to basic and key industries coming under "Planned" development;

(c) "Commercial" industries should be protected if

  (i) its comparative cost of production is such as to enable it to achieve sufficient efficiency within a reasonable time so as to enable it to carry on without protection or assistance,

  (ii) it is an industry to which it is desirable to extend protection in the national interest.

Fiscal policy during the last decade has recognised that prior establishment is not essential to obtaining protection and that anticipatory protection can, and should, be granted to those industries which require heavy capital investment or whose products are so highly specialised as to limit the mobility of its personnel.

5·5 The establishment of a permanent statutory Tariff Commission by the Tariff Commission Act of 1952 was a major step forward in setting up a specialised machinery for continuously watching the working of the protectionist tariff. The Act enjoins on the Commission functions wider than mere "tariff protection" and lays stress on the developmental aspects of protection. The Commission has broadly the following functions:

(a) inquire into claims for initial protection,

(b) examine the case for continuation of protection,

(c) review periodically the working of protection particularly with reference to production, costs and prices of protected industries,

* For an analysis of the importance of Industrial Development, See Vol. I pp. 222—226.

(d) undertake price-fixation enquiries, for commodities whether protected or not,

(e) advise government on matters relating to imposition of anti-dumping duties and retaliatory measures, and, negotiations of trade agreements and tariff concessions.

The powers of inquiry and advice can be exercised by the Tariff Commission only on a reference being made to it by Government, except in cases of continuance of protection where the Commission is empowered to make a *suo moto* review, and recommend modification or abolition of protective duties which during the period of protection can be altered only on the advice of the Commission.

5·6 *Arguments for Protection*[102]. The academic controversy between Free Trade and Protection is perhaps as old as trade between nations. It is, however, doubtful whether in any country technical bodies entrusted with the task of advising on tariff-making have in fact approached the question from any of the more general arguments advanced by protectionists. It is generally believed that the older approaches to the question of protection have now been outmoded as a result of the growth of planning and that now-a-days an underdeveloped country seeking to raise its level of living by planned effort must regulate its foreign trade and promotional efforts relating to its indigenous industries in accordance with the broad objectives of planning. The more important questions now relate to the economic objectives capable of being attained through a protectionist-tariff, while theoretical arguments to justify the adoption of a protective fiscal policy have been relegated to the background. Fundamentally, of course, it still remains true that inefficient industries cannot be bolstered up except through permanent extra burdens being imposed on the consumer so that successful protectionism does involve the conversion of indigenous industries ultimately into positions of comparative advantage. In a sense, therefore, the case for protection is not a general one, but one dependent upon the favourable potentialities of intervention by the state on behalf of particular industries where the specific circumstances of time and place are conducive to efficient growth. The arguments for protection have been succinctly stated[103] as follows :—

"A scientifically designed tariff equalises the production costs of the home and foreign producer ;

102. See Coyajee—Indian Fiscal Problem, Lecture I.
103. Mcguire—The British Tariff System, p. 88.

assistance is given to nascent and temporarily depressed industries; home markets are created and existing markets are stabilised; it assists the formation at home of large producing units which are better able to compete with the foreigner in the world markets; and that where the home market is important to the foreigner, it induces him to sink money in the country in order to retain it. As a consequence, employment is increased; wages tend to rise and idle capital and labour are brought together. Hence greater prosperity will result behind the tariff barrier and the receipts from direct taxes will swell, so that the need for revenue from imports will become less urgent. Further, the protective tariff will strengthen the bargaining power of Government in its efforts to obtain access for the domestic products in the foreign markets, and, therefore, assist in any endeavours towards a general lowering of the tariffs. If, in addition, the Government is permitted to discriminate with rates against imports from particular countries, it has greater power of retaliation when the nation's tariff is politically expedient to ensure the maintenance of certain key industries within the country in order to preserve the safety of the State in time of war."[104]

5·4 *Working of the Protective Tariff*. The Tariff Commission, in spite of the variety of weighty factors which it refers to in the course of its reports, has, in the last analysis, based its method of tariff protection on costs. The basic approach of the Commission has been to compare its calculated fair ex-works cost of production of indigenous manufactures with the (c.i.f.) costs of competing imported commodities, and to determine the quantum of protection on the difference. In short, the Commission has been influenced considerably by cost of production analysis, though over the period of the last decade various refinements have been attempted in its cost analysis. The Commission's main difficulty has been to allow for variations in cost, regionally or between individual producers. They have attempted to solve the problem by taking the ex-works costs of what the Commission termed "representative"* units of the industry, and, arriving at what they regarded as a representative "fair-selling price." It is difficult to assess the accuracy with which the Commission were

104. See also Haberlar Theory of International Trade, Chapter XVI and XVII.

* Not to be confused with the Marshallian idea of a Representative Firm.

able to determine the quantum of protection needed, for the period 1952-1962, which constituted the decade of the Commission's activities also was a decade of strict import control on the whole, so that it is difficult to separate the protective effect of the tariff and the protective effect of severely limited competing imports. In fact, the short period within which a fairly large number of industries were deprotected could be explained perhaps as much by the continued protective effect of import control as by possible improvements in efficiency and reduction in costs of production. The unusually high level of the revenue tariff has also undoubtedly contributed to a protective effect for it is well-know that in many cases the Tariff Commission merely suggested conversion of the existing revenue duty to a protective one. In some quarters there is a tendency to take up the highly fallacious attitude that "Import-control measures are in no sense part of the scheme of tariff protection." If by such a statement it is intended simply to imply that import-control is not actuated by a specific desire to provide protection in the traditional sense of the term, then it is fatuous ; if any other sense is implied, it is wrong.

6. Commercial Policy and Trade Agreements.

6·1 Recent trends in foreign trade and difficulties in our balance of payments have focussed to the forefront development in our commercial policy because external trade today constitutes one of the most strategic factors in the programme of India's economic development. It is being increasingly recognised that the Balance of Payments of a country—least of all of one engaged in a gigantic experiment of planned development—is not an autonomous entity ; it is only a reflex of the relationship between its internal economy and the rest of the world. There may be need, specially in the short period, to attempt to influence the balance of payments position (partly in the quantitative sense, but mainly in regard to the factors determining its composition and countrywise allocation) by adopting devices like exchange controls, tariffs and trade agreements, State trading, large-scale international movement of funds and "aid" programmes from friendly countries. It might be clarified that such a commercial policy, designed to influence the balance of payments position, need not necessarily be directed towards a reduction in imports. A programme of industrial development would normally require large imports of machinery and equipment, which may, in fact, increase the total volume of imports. As industries are gradually established, the type of imports would undergo a further change, and, intermediates and semifinished goods

would replace manufactured imports. To start with, much of capital imports must be borrowed, necessitating in course of time an export surplus for repayment. The position was well summed up by the expert team of bankers for the World Bank[105] in the following words :—

"The emphasis given in the programmes of industrial development to import saving by no means implies, however, that the import requirements of India will necessarily follow a declining trend over the next 5, 10 or 15 years. On the contrary, it is likely that as the Indian economy moves towards progressively higher stages of development, new types of import required to sustain this progress will outweigh the economies achieved in other areas. The greater the pressure for rapid industrialization and general economic development, the greater the likelihood that there may be a progressive racheting upward of import requirements. This further underlines the necessity of giving high priority to the investment of effort, money and talent to the export field where the development of markets often takes a considerable time."

6·2 To the above one has only to add a ultimate repayment burden of India's foreign liabilities and interests thereon to realise the large export-surplus that would be needed in course of time. It seems, therefore, necessary to diversify our exports, for with growing competition from producers in other countries and greater intensification of dangers from growth of substitutes, we might find our vulnerability rather dangerous if we continue to rely on a few basic traditional items as we have been doing in the past. In this context, however, we must recognise that a major factor affecting India's trade over the coming years stems from the trading and commercial relations which are being developed through our commercial treaties and agreements relating to trade with individual countries. It has been claimed that "the total value of trade with trade agreement countries has been on the increase at faster rate than overall trade. Exports to countries with whom we have trade agreements increased from less than 67 percent of the total in 1957 to 72 percent in 1959; the total value of exports to these countries being as much as Rs. 449 crores out of a total of Rs. 623 crores during 1959. Exports to East European and North Asian countries have increased over the past few years from the negligible amount of Rs. 7 crores in 1954 to Rs. 54 crores in 1959, largely through trade agreements concluded with these countries."[106]

105 Letter to the President, International Bank for Reconstruction and Development from the members of the International Economic Mission, March 1960.

106 Sri S. Ranganathan, Commerce Secretary, vide article in Problems in the Third Plan, p. 117.

It should, however, be borne in mind that growth of exports to 'trade agreement' countries is, by itself, not very important if it simply represents a diversion of exports from one area to another. Such beneficial results for trade-agreements should be more appropriately be claimed only if a total increase in our export earnings takes place, and, it is doubtful whether any significant part of the increase in our export earnings was in reality due to these agreements.

6·3 *The General Agreement on Trade and Tariffs (G.A.T.T.)* India is one of the original signatories to this agreement which aims at a general reduction in tariffs and promotion of multilateral trade and payments. It has been possible for India to obtain valuable tariff concessions from several countries and thereby expand her trade. When the General Agreement was originally signed, India had not embarked on ambitious plans of economic development. The period 1950-55 however, marked the beginning of a new era of attempts at rapid economic development in under-developed countries through government sponsored economic planning. It was obvious that under-developed countries could not be expected to grant reciprocal concessions under the G. A. T. T., if such concessions adversely affected their development plans. Accordingly it was agreed in 1955 by its ninth Review Session that under-developed countries could impose sufficient quantitative restrictions on their imports to conserve and build up their foreign exchange resources to be utilised for their economic development programmes. Thus Article 11 of the G.A.T.T. gives the fullest scope to the Government of India to restrict imports, if such restrictions were necessary to safeguard the balance of payments position—the manner of imposing the restrictions and commodities on which they are to be imposed being left to the discretion of the Government of India. This facility, together with the original principle of exclusion of protected industries from the automatic operation of concessions, has enabled India to ensure that concessions granted are demonstrably in the interests of national economy. Finally, the G.A.T.T. does provide for promotion of freer trade and elimination of preferentialism in international trade. It provides that whatever concessions are granted to one country must be immediately and automatically extended to all the contracting parties, so that the membership of the G.A.T.T. obviously enables India to obtain the most favoured nation treatment from all the contracting parties. This is bound to be a valuable source of strength when our export-receiving countries undertake tariff negotiations with our economic competitors.

6·4 ***Trade Agreements.*** **It has already been pointed out**

that trade agreements have been playing an important role in our foreign trade, particularly in promoting exports. The following are some of the more important agreements undertaken in recent years:

(a) *1958-59*: A new agreement was concluded with Ethiopia, U.S.S.R. and Iraq. The period of validity of the agreement with U.S.S.R. is for five years, while the other two are only for one year. Agreements with many other countries were extended or modified. The chief purpose of the agreements has been the ensuring of a balance in our bilateral trade. They also attempted to enlarge the markets for Indian exports. The mechanism for achieving these ends was threefold, viz.

(i) providing for payment for imports in non-convertible rupees, thus ensuring that they are used for the purchase of Indian goods;

(ii) providing credit arrangements to facilitate purchase of Indian goods; and,

(iii) fixing monetary or quantitative ceilings for imports and exports.

The other important agreement to be signed during 1958-59 was with the U.S.A. providing for the import of wheat against export of manganese ore and ferro manganese.

(b) *1959-60*: The old agreements with China, Greece, Hungary, Indonesia and Viet Nam were extended for varying periods and new agreements were concluded with a large number of countries, chief of whom were Bulgaria, East Germany, France, Italy, Poland, Switzerland and Yugoslavia. Broadly the provisions were as follows:

(i) the East European Countries would receive payment in non-convertible Indian Rupees,

(ii) the West European Countries would take larger Indian exports so as to correct the imbalance arising out of larger imports from these countries into India.

An interesting agreement concluded during the year was the one with the Misr Foreign Trade Company, Cairo, providing for the purchase of rice in exchange for sale of tea, jute goods and certain minor items of exports which were mostly non-traditional.

(c) *1960 61*: Five of the older agreements were renewed and four others were modified to India's advantage. New agreements were concluded with Morocco and Tunisia while a ten-year Treaty of Trade and commerce with Nepal, which

expired on 31st October, 1960 was replaced by another. The various agreements continued to be used as instruments for reducing the imbalance of India's foreign payment situation and strove to stimulate our exports by developing trade with fresh markets and new commodities.

The total number of trade and payments agreements in force at the end of 1960-61 was 26 and covered practically all the important trading countries of the world.

7. State Trading.

7·1 The Third Five Year Plan has reaffirmed faith in State Trading, stating that "State Trading has to be undertaken on an increasing scale according to the needs of the economy." There are indications that State Trading would be extended in suitable directions, particularly in developing exports. It would appear that faith in the efficacy of State trading has been on the increase, and whatever might have been the origin, at present the increasing part played by it is not so much due to ideological reasons as its having established itself as a potent and effective weapon for furthering the country's economic development and economic policy. This has been made possible by the spectacular results achieved by the State Trading Corporation established in 1956.

7·2 Development of the idea of State trading in India has been a slow progress. In fact, it has a chequered history, the idea finding favour with one Committee and being treated with considerable scepticism by another. In view of the pronounced tendency towards a socialist pattern of society as an ideology, the government has, since independence, attached considerable importance to the concept of State trading. As early as 1949, a committee was appointed to go into the question. This committee was in favour of State trading and recommended :

- (i) establishment of a Statutory Corporation for undertaking the activities of State trading,
- (ii) undertaking by such a Corporation the trading activities relating to
  - (a) foodgrains and fertilizers,
  - (b) departmental imports and exports of a commercial nature,
  - (c) import of East African cotton and export of short staple cotton,
  - (d) export of products of cottage industries.

The committee favoured the idea of raising revenues for

the State through profits on State trading. In this respect it was only anticipating the idea later adopted in our planning literature that surpluses of government commercial undertakings were a legitimate source for investible funds.

Subsequently, during the later phase of the First Five Year Plan, another committee was appointed* to go into the question. This committee took up an opposite view and held that conditions in the world market had altered so much as to make it unnecessary to establish a State trading organisation to import foodgrains, cotton and fertilizers. The committee, however, considered that in a limited sphere, like export of products of small scale and cottage industries, there was scope for State trading. In short, this committee considered State trading more as a means to prop up specialized exports for helping comparatively antiquated production methods rather than as an overall measure of governmental policy for regulating trade.

7·3 The Taxation Enquiry Commission[107] of 1953-54 approached the question of State trading from the revenue point of view and came to the conclusion that "no spectacular results may be expected from State trading over a short period." Their conclusion was based on their assessment that

(a) the governmental machinery was inadequately equipped to handle such responsibilities,

(b) such operations were suitable when prices were rising

The T. E. C. distinguished between State trading in the field of foreign trade and internally, regarding the latter as an aspect of fiscal monopoly. In the case of internal trade also they were inclined to the view that lack of expert personnel might operate against their success.[108]

7·4 *Functions of the State Trading Corporation.* The Corporation was incorporated under the Companies Act and was registered on 18th May, 1956 with Government holding the entire capital.

The objects for which the company was established are :

(i) to organise and effect exports and imports into

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* The first Committee was presided over by Dr. P. S. Deshmukh while the second Committee had as its chairman Shri S. V. Krishnamurthy Rao.

107. See Report Vol. I, pp. 207-09.

108. Compare with view expressed in Vol. I, pp. 217-19 regarding State Trading in foodgrains.

India of all such goods and commodities as may be determined by the Company from time to time, and to undertake the purchase, sale and transport of and general trade in such goods and commodities in India or anywhere else in the world ;

(ii) to acquire and undertake the whole or any part of the business, property and liabilities of any person or Company and to improve, manage, develop, grant rights or privileges in respect of, or, otherwise deal with all or any part of the property and rights of such person or company ;

(iii) to subscribe for, take, or otherwise acquire, and hold shares, stock debentures or other securities of any other company ;

(iv) to give guarantees and indemnities for the performance of contracts in which the Corporation is interested ; and

(v) to do all such other things as are incidental or conducive to the attainment of the above objects.

It is obvious that a Government owned and Government controlled organization like the S. T. C. must become in course of time a powerful economic entity and use its monopolistic position to derive large profits of the nature of extra-Parliamentary source of taxation. From the point of view of pure theory of public finance there can be little objection to the making of such profits through inflation of various elements of cost included in the price. Such profits would be a much needed addition to resources required for planned development. Whether, politically it is incumbent that if such additional revenue is to be raised, it must be through specific taxation measures levied with the approval of the representatives of the people, i.e., Parliament, rather than by charging high prices, is a question which does not interest the student of public finance or economic development. In pure theory, further, the S.T.C. is not merely an agency for raising additional revenues; it is also an agency to arrange for procurement and distribution of scarce commodities in the interest of the consumer. However, it must be admitted that the S.T.C. has not always been successful in protecting the interests of the consumers for "The gaps between supply and demand which persisted caused a heavy strain to the distributing mechanism with the result that it was not always possible to ensure sales at the prices fixed by the Corporation,[109] i.e., the S.T.C. could not, in effect; prevent black marketing.

109. Third Annual Report of the S.T.C.

7·5 *S.T.C. and Foreign Trade.* There is a feeling, particularly amongst traders and industrialists in the private sector, that the S.T.C. should confine itself to trading with countries where trade is canalised through State channels. It is difficult to accept such a contention. The S.T.C. is an additional organ of trade to give effect to some of the economic policies of Government. While trading with State Organisations and with monopoly organisations of other countries might be a particularly suitable aspect of its activities, neither the objectives with which it was set up nor its subsequent role justifies such a narrow interpretation of its functions. It might be pointed out that in the realm of foreign trade the part that the S.T.C. is expected to play is very wide and was summed up admirably authoritatively[110] as follows:—

(a) monopoly import of specified commodities,

(b) trade with totalitarian countries i.e. those whose trade is canalised through State channels,

(c) trading with monopoly organisations in other countries,

(d) promote trade on link basis,

(e) promote exports and diversify foreign trade,

(f) make compensating transactions by arranging for import of one commodity and export of other commodities,

(g) enter into barter deals.

The S. T. C. has, with a view to furthering the above functions, entered into special agreements and trade plans to secure a 'balanced basis'. Some of the recent agreements of this type are the following:

1958-59: Agreements with foreign trade organizations of Czechoslovakia, Hungary, Yugoslavia and Mongolia. The specific feature of these agreements was the stipulation to effect or actively facilitate exchange of specified commodities.

1959-60: Agreements with trade organisations (both state associated or private) of China, Italy, Japan, Lebanon, Switzerland and Viet Nam. These agreements were designed actively to facilitate the exchange of specified commodities. They further attempted to secure certain essential imports and to open up wider and newer markets for India's exports, especially the non-traditional items of exports.

The volume of business handled by the S.T.C. during 1st April 1959 to 31st March 1960 is as follows:

110 Estimates Committee of the Lok Sabha, Eighty sixth Report.

Exports	Rs.	1662·67 lakhs
Imports	Rs.	2844·17 lakhs
Total	Rs.	4506·84 lakhs

The recent Report[111] of the Import and Export Policy Committee (of which the chairman was Shri A. Ramaswami Mudaliar) examined the grievances of the private sector carefully and stated :

> "We have carefully analysed the programme of the Corporation's work over the past few years. It seems to us that much of the criticism against the S.T.C. stems from a misconception of its role and functions ...."

7·6 *Summary of Financial Position of S.T.C.*

	1957-58 Rs.	1958-59 Rs.
1. Capital subscribed and paid by Government of India ...	1,00,00,000	1,00,00,000
2. Other than by Government of India	...	...
3. Borrowings	2,46,68,377	3,01,52,549
4. Free reserves and surplus ...	1,30,00,000	2,58,72,128
5. Other liabilities ...	4,16,67,685	9,39,87,105
6. Total 1—5	8,93,36,062	16,00,11,782
7. Gross fixed assets ...		
8. Depreciation		
9. Net fixed assets ...	6,46,537	6,58,053
10. Stocks and stores/Current assets	2,89,76,856	8,11,80,316
11. Outstanding, advances, and investments	4,54,02,184	7,59,62,084
12. Other investments including cash	1,43,10,485	21,71,329
13. Losses (Total)	...	...
14. Total 9—13	8,93,36,062	16,00,11,782
15. Wage bill for the year (Rs.)...	31,00,000	41,78,000
16. Number of persons employed (actuals)	1,221	1,573
17. Interest charges during the year (Rs.)	5,36,750	10,35,566
18. Net profit for the year before taxation (Rs.)	2,13,08,889	3,32,78,933
19. Value of output in the year (Rs.)	28,38,03,124	38,57,87,114
20. Value of sales (Rs.) ...	28,57,61,882	35,95,02,643
21. Government subsidies if any, (Rs.)	...	...

N. B. Accounting year July—June Source C.S.O.

111 Report submitted on 28th February 1962, p. 44

7·7 S. T. C. and Economic Welfare. In pure theory, one could conceive of the S. T. C. playing an important role in promoting economic welfare of the country. It could bring about a saving in foreign exchange and help in lessening the adverse balance of payments. It could, by promoting exports and diversifying foreign trade, help to make our terms of trade more favourable. By entering the market, it could help to stabilise prices, at least of the more important essential commodities. It could even be the agency to arrang for procurement and distribution of scarce commodities in the interest of the consumer. It could do all this and probably more; the ardent advocate of State participation in economic life regards the S. T. C. as the custodian of trade policy just as the Reserve Bank is the custodian of monetary policy. Planners all the world over, and particulary in India (because of the paternal official outlook and an unbounded confidence in the knowledge and ability of our services), hold the view that trade in general, foreign trade in particular, can always be managed more efficiently by the State than by private enterprise. This view has been further strengthened by the Constitution of India enjoining the State to secure "that the operation of the economic system does not result in the concentration of wealth and means of production to the common detriment." In fact, the whole concept of the relative roles of the public and the private sectors is undergoing a change, and, the two are being increasingly looked upon as parts of a single organisation under a Planned Economy rather than as separate entities.* There is, therefore, every reason to believe that the State can successfully intervene in economic life to promote welfare, and limitations of administrative adaptability are merely short period practical "brakes" rather than insurmountable obstacles. The S. T. C., however, is still only a marginal influence. The total volume of trade handled by it is estimated now to be about Rs. 60 crores,[112] which is an insignificant proportion of our national dividend. It has not so far obviously reached the point where it can be said to be in a position to effectively modify the economic situation as a whole. But it is a potential power, and like all potentially powerful weapons, it can be used for good or evil. Whether it would become in course of time only an irritating fifth wheel in the chariot of progress or will be an efficient channel for giving effect to the economic policies of Government remains to be seen. One must, however, bear in mind that the inexorable forces of economic life are not always either easy or even

* See Vol. I, pp. 22—25, 30—32.

112. Report of the Import and Export Policy Committee ch V, para 13.

possible to dictate. There are also limitations of knowledge and information available. Loose thinking sometimes prompts one to assert that State Trading can achieve miracles, that it can bridge the gap between demand price and the cost price. Behind such facile claims is the misconception that Government are aware of the demand and supply situations, and, therefore, can suitably adjust the price of the products in which it trades so as to minimise the gap. Such, however, is not the case and one should not pursue a mirage riding on soap-bubbles.

8. Terms of Trade and Indian Foreign Trade.

8·1 The primary measure of a country's economic gain from international trade is its terms of trade, and, the favourable or unfavourable movement of the country's terms of trade. The measure which is the simplest and the most frequently used is the ratio between export prices and import prices. Since costs are not constant, the prices of different export goods (or import goods) will not indicate parallel movements. This leads to difficulties in statistical measurement and compels use of averages of export-prices (and import prices). In a sense, therefore, movement of terms of trade—for or against—may give an illusory index of gain or loss; i.e. like most statistical proofs they may hide more than they reveal, but as illustrative of likely increases or decreases in benefits from foreign trade, they are useful on the assumption that other things remain equal. Of course, it is elementary knowledge that an adverse movement of terms of trade is merely indicative of a reduction in benefit from international trade and not of loss from it, unless, of course, it were necessary to continue it because of compelling non-economic considerations.

8·2 Arguments are often advanced to claim that diversity in export trade is desirable to improve one's terms of trade; again, it is often argued equally forcefully that concentration on a few articles tends to create conditions akin to a monopolist supplier and enables realisation of better terms of trade. Both views are fallacious. A country's position is not necessarily more vulnerable merely because its exports are made up of a few traditional articles; nor does it necessarily have a weaker bargaining position because of a large number of export items each contributing a small proportion of the total export-values. Usually the concept of the terms of trade implies :

$$\frac{\text{Index Number of Export-Prices}}{\text{Index Number of Import Prices}} \times 100$$

The index so derived is compared with that of the base year (=100), and, it is roughly possible to indicate whether terms of trade are becoming more or less favourable, bearing in mind that the basis is to regard the terms of trade in the base year as normal. The comparison, however, becomes rather unsatisfactory when a substantial shift takes place in the composition of a country's trade from agricultural to industrial commodities or *vica versa*.

8·2 Readjustments of foreign trade do not take place in the very short period so far as composition and direction of trade is concerned. The immediate effects on foreign trade, therefore, are from changes in prices and the movements in terms of trade are usually the outcome of price-changes. Taking 1948-49, as the starting point (India in the present sense came into *existence* on 15th August 1947), we find the position in the first two years of the trade of Independent India as follows :

Year	Import price Index	Export price Index	Net terms of Trade
(1)	(2)	(3)	(4)
1948-49	346	395	114
1949-50	330	389	118

Source : Reserve Bank of India Bulletin, July 1950.

Looking at details, we find that terms of trade were most favourable to us in May 1948. However, they moved against India till early 1959. There was an increase in the volume of Imports as also a rising difficulty in our balance of payments. The volume of exports declined, particularly of spices and raw materials where the export-prices were usually higher than general level of prices.

8·3 We have studied earlier the nature of our balance of trade and our balance of payment during the decade 1950-1960. The last decade constitutes a decade of planning and, as pointed out earlier, the needs of planning exerted considerable influence on the quantum of our foreign trade as also on its composition and direction. As a result, our terms of trade moved against us for sometime. The adverse movement continued till 1957, and though there has been recovery thereafter, both 1958 and 1959 continued to have terms of trade which were more unfavourable than we had in 1950. The figures for the midyear of 1960 (i.e. July 1960, which is

the latest available for comparative study)* shows a definite favourable swing. The following figures illustrate the position :

India's Terms of Trade

(Base : 1953 = 100)

	1950	1955	1956	1957	1958	1959	July 1960
Export Prices	98	100	101	101	100	98	109
Import Prices	90	93	94	104	97	95	94
Terms of Trade	109	108	107	98	103	103	116

8·4 *The Future.* A precondition of our planned economic development as visualised in the Third Five Year Plan is a high import-surplus. This inevitably implies that when the urgency for heavy imports is reduced, an export surplus will have to be built up to repay the maturing credits. Of course, the need for such surpluses in the immediate future may not be much, but they gradually increase until they acquire significant proportions. It is clear that "aid" ought to be accompanied by trade, and, creditor countries must take substantial exports from India as it is unlikely that the old concept of multilateral free trade would ever revive sufficiently to enable India to achieve an adequate export surplus otherwise.

* The Reserve Bank of India Bulletin. e.g. March 1962 gives in table No. 54 information on terms of trade for 1959 onwards with 1958-100 ; one wonders why it was necessary to have a new index with 1958 as base.

IX

MONEY, CURRENCY AND PRICES

1. The Monetary System—its nature since 1947.

1·1 In no field of economic thinking has there been more profound change than in the concept of the monetary standard. Earliar ideas of convertible currencies, particularly links to gold or international free convertibility, have more or less been abandoned ; in fact, even the common man hardly bothers as to whether the medium of exchange that he handles everyday is ultimately anything more than a mere token, and students of economics rarely now need worry about the distinction between "face value" and "intrinsic value" or the significance of "true money" *vis-a-vis* "fiat money". In this field of our study, therefore, it is futile to go back into history for the rupee to-day is, in reality and in effect, an inconvertible currency with no ultimate internal convertibility in terms of anything other than money, while its external convertibility is hedged in with such severe measures of exchange control as to cease to have any significant practical importance as a general characteristic.

1·2 The beginnings of a modern monetary system for India were laid on 1st March 1947 when India became a member of the International Monetary Fund. With the establishment of the I.M.F. , the world more or less abandoned its old love, the Gold Standard, and entered into the new era of managed money. Prior to this crucial date, India had what was commonly known as the Sterling Exchange Standard, with the Reserve Bank of India maintaining a foreign exchange rate of 1sh 6d for the rupee. In a sense, the more or less revolutionary change which took place with India's joining the International Monetary Fund did not really cause a complete break from the past for under the new system, the rupee obtained (or rather, was given) a gold parity rate through the I.M.F. which maintained the old rate of 1sh 6d for the rupee. The new parity rate, it might be emphasised, was a decision of I.M.F. and the Government of India through

the Reserve Bank of India. The change, however, was subtle, and while in theory the rupee continued to be convertible into any foreign currency, in reality its convertibility was subject to the provisions of Exchange Control Act of 1947. Thus an interesting paradox began to exist, *viz.*, while the issue department of the Reserve Bank of India was required, under the law, to hold Sterling as well as other foreign currencies (to enable, presumably, multilateral external convertibility), the law relating to exchange control made it impossible to have such convertibility freely, especially in terms of the dollar (and other specified currencies) brought under the purview of the Exchange Control Act.

2. The Currency System at Present.

2·1 Basically, India to-day has an inconvertible paper currency, for the Indian rupee is internally not convertible into anything except itself ultimately *viz.* the one-rupee note. One could, of course, get small change but the face value of our small change coinage is much higher than its intrinsic value making it as much an inconvertible coin as the paper-note. In any case, limited convertibility in terms of small change does not contribute to convertibility as such which in traditional economic theory implied the ability of the holding public to reduce (or expand) the supply of money on its own initiative in response to its requirements of trade.

2·2 The one-rupee note, the minimum unit of currency in the country with legal tenderability, is issued by the Government of India. All other denominations of paper currency are issued by the Reserve Bank of India, which has a special Issue Department for the purpose. The unwary student of economics may often be surprised by figures of "Rupee Coin in Circulation" issued by the Reserve Bank of India. It is necessary to bear in mind that since June 7, 1947 all standard rupee coins had ceased to be legal tender in India. The term "Rupee Coin in Circulation", therefore, now implies a total comprised of

(i) Government of India one-rupee notes issued from July 1940,

(ii) Quarternary silver rupees issued between December 1940 and June 1946, and

(iii) Nickel rupees issued from June 1947

Of the above, quarternary silver rupee coins are in the process of being withdrawn, it being estimated[113] that out of

113 Vide Reserve Bank of India, Report on Currency and Finance, 1960-61.

a total of Rs. 94 crores of such coins outstanding on the date of discontinuance of their issue, coins of the value of Rs. 61 crores had been retired upto March 31, 1961. Thus the phrase 'circulation of rupee coins today in India means that the bulk it represents one-rupee notes. Further, since none of the constituents of the rupee circulation in India is convertible internally into gold or silver, and since they are not "self-convertible" by "melting", due to their face value being much in excess of their intrinsic value, the ultimate internal inconvertibility of the Indian currency is self-evident.

2·3 The note-issue in India was originally based on what may be termed as a sort of a "Proportional Reserve System". According to the original provisions of the Reserve Bank of India Act, 1934, it was incumbent on the Bank to maintain not less than 40 percent as reserve in gold coins, gold bullion or Sterling Securities. The 1934 Act further laid down that the value of gold coin and gold bullion included in the 40% reserve was not to fall below Rs. 40 crores. The remaining 60 percent of the reserve—which covered what may be called the fiduciary portion of the issue—was to include Rupee coins, Government of India Securities, approved bills of exchange and promissory notes, subject to the further provision that the amount of Government securities held could not exceed a quarter of the total assets or Rs. 50 crores, whichever was greater. This was the method of regulating note issue when India had a Sterling Exchange Standard, a currency standard which was in a sense ideally suited to India in view of her not having an independent financial centre of International importance and in view of her substantial trade links with U.K. and sterling area countries, though it undoubtedly did involve a considerable measure of dependence on sterling. With India joining the International Monetary Fund in 1947, it was necessary to amend the law to include foreign currencies other than sterling in the reserve, and this was done by suitably amending the relevant provision of the Act.

2·4 The proportional system of note-issue that the 1934 Reserve Bank Act prescribed was not strictly a "percentage" system of regulating note-issue. Under a percentage system gold reserves were not to fall below the prescribed percentage of the note-issue, the intention being to ensure convertibility. The Indian system, by permitting sterling securities to be included in the 40 percent portion along with gold coin and gold bullion was strictly not a "percentage" system, though it undoubtedly did provide for a minimum value of gold coin and bullion to be held. However, the variation introduced probably made the Indian system a little

less unscientific than the "percentage" system for which the late Lord Keynes[114] saw "no sound foundation in logic or common sense", and which, according to him "appears to combine all the possible defects of systems of note regulation."

2·5 Recent amendments have moved the system of regulating note-issue further and further away from the so-called fashionable "percentage" system. In 1956, an amendment was undertaken which provided that the minimum reserve of gold coin and bullion should be of the value of Rs. 115 crores. The gold held was also revalued and separate lower limits were provided for the reserve held in (a) gold, and (b) foreign securities. The amended provision enjoined that the Issue Department of the Reserve Bank of India must maintain

(a) Rs. 115 crores in gold, and,

(b) Rs. 400 crores in foreign securities, though this could be reduced, under special circumstances to Rs 300 crores.

In 1957, an Ordinance was issued by the President which further amended the relevant provision of the Reserve Bank Act and reduced the minimum currency reserve in foreign securities. The new provision made the following arrangement :

(a) overall minimum reserve to be Rs. 200 crores, of which

(b) gold coin and bullion to be not less than Rs. 115 crores.

Thus the amendment implied that the effective legal minimum for foreign securities was to be only Rs. 85 crores, while the gold portion of the reserve was to continue to be governed by the minimum limit of Rs. 115 crores.

2·6 The Liabilities (notes issued) and Assets (gold. rupees and securities, foreign and Indian) of the Issue Department of the Reserve Bank of India indicates the relative movements of the reserves held to changes in total note-issue. The statement given below summarises the position :

114. J. M. Keynes—Treatise on Money, Vol. II, p 268.

Reserve Bank of India
(Issue Department)

(In lakhs of rupees)

	(A) LIABILITIES		Total	(B) ASSETS			
Year	Notes in circulation	Notes held in Banking Department	A or B	Gold coin and bull-ion	Foreign Securities	Rupee coin	India Govt. Securities
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
1951-52	1,189,84	27,78	1,217,62	40,02	625,27	63,98	488,36
1955-56	1,339,39	17,08	1,356,47	40,02	656,52	106,87	553,06
1958-59	1,593,88	19,34	1,613,21	117,76	182,04	133,99	1,179,42
1960-61	1,863,13	18,94	1,882,07	117,76	134,99	126,84	1,502,48
June 1961	1,958,79	30,43	1,989,22	117,76	108,01	118,54	1,644,92
Dec. 1961	1,937,46	14,76	1,952,22	117,76	116,86	122,78	1,594,82
Feb. 1962	2,022,55	18,28	2,040,83	117,76	126,11	119,51	1,677,45

Source : Reserve Bank of India.

Two points regarding the above table need to be clarified. First, the concept of the term "rupee coin" should be borne in mind as it mainly implies one-rupee notes rather than coins as such (vide para 2·2 above). Secondly the large increase in the value of gold (column 5) noticeable after 1955-56 is due not to any increase in the quantity of gold holdings but to a revaluation of gold reserves undertaken on October 5, 1956. The gold reserves of Issue Department were previously valued at Rs. 21·24 per tola and were valued at Rs. 62·50 per tola after 5th October, 1956. Thus, the gold holdings of the Reserve Bank of India have remained constant in terms of weight throughout the period.

2·7 The internally inconvertiible Indian currency system is in accordance with modern concepts of scientific currency standards, for to day internal convertibility in terms of precious metals is regarded as a relic of the crude money age when lack of confidence in the management abilities of monetary authorities led to emphasis on such convertibility as a desirable feature. Modern monetary theory, however, lays greater emphasis on the function of money as a medium of exchange and recognises that for discharging this function

efficiently it is neither necessary nor desirable to make money internally convertible. It is being increasingly emphasised that adjusting money supply to the requirements of the economy is essentially a function of monetary management and that in the hands of an efficient monetary authority managed money adjusts itself to requirements far more quickly and appropriately than it would do through the so-called automatic forces of a convertible gold standard.

2·8 The law relating to note-issue in India still requires the maintenance of a gold reserve. It might be useful to recognise clearly the true function of a gold reserve in a currency system which is internally inconvertible and which operates in an international trade structure that sevenely limits multilateral (even bilateral) convertibility of a country's currency. In the traditional Gold Standard, movements of gold adjusted discrepancies in balance of payments, and, by influencing money-supply consequentially, brought about an altered condition of costs and production that led to readjustments of quantities of exports and imports, and capital movements, so as to correct the balance of payments position The gold reserve of the Central Bank had, under the Gold Standard, the function of assisting in the maintenance of internal convertibility and external stability of the country's currency. Such cannot be the function of the Reserve Bank's gold reserve for the rupee has no internal convertibility, nor apparently has the reserve played any effective part in regard to external stability for the quantity of gold reserve has not been altered during the last decade. Perhaps, the gold reserve of the Reserve Bank of India is being held, fortuitously if not deliberately,

> "Partly, to provide liquid resources for use in ultimate emergencies........; partly, for merely psychological reasons to promote confidence..."[115]

3, Money Supply.

3·1 *The Concept*. Recent rise of prices has focussed attention on the important question of total money-supply with the public. A period of rising prices invariably revives interest in the traditional quantity theory of money wherein inflation was held to be the result of increases in money-supply. Without going into the intricacies of the theory of value of money, it would be useful to understand the changes in the money supply with the public during the last decade and the various factors which account for them. The con-

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115. For a highly theoretical discussion of the object of a gold reserve, see, Keynes—Treatise on Money, Vol. II, pp. 273-277.

cept of total money supply with the public represents the total of currency in the hands of the public and the demand deposits of banks. It indicates the total volume of monetary media of exchange available to the community for use in connection with the economic activity of the country. As students of economics are well aware, the actual level of money supply at any given point of time is not so important as its variation over time.[116]

3·2 *The Volume* : The table given below indicates the position in this respect :

Money Supply with the Public

(Crores of Rupee)

Last Friday of year	Currency with the Public	Deposit Money with the Public	Money Supply with the Public (2+3)	Variation in Money Supply with the Public
(1)	(2)	(3)	(4)	(5)
1950—51	1,330·76	640·30	1,971·06	+112·65
1955—56	1,505·22	679·23	2,184·45	+264·26
1956—57	1,556·49	756·39	2,312·88	+128·88
1957—58	1,607 13	782·22	2,389·35	+ 77·12
1958—59	1,725·36	774·23	2,499·59	+109·91
1959—60	1,862·72	840 41	2,703·13	+204·97
1960—61	2,026·89	874·83	2,901·72	+201·47

Source : Reserve Bank of India

N. B. Col. 2 excludes circulation of small coins, but Col.5 includes variations in its circulation; hence, the slight difference in the figure of Col. 5 as compared to the year to year difference in Col. 4.

It is necessary to understand the composition of the items included in columns 2 and 3 of the above table. But before analysing these componets, one interesting feature of the situation in India may be pointed out, *viz.*, the preponderating significance of "Currency" in our Country. In India Column 2 is practically the determinant of Column 4 ; on the other hand, in the developed Countries where the banking habit is more fully developed, currency constitutes a relatively minor proportion of money supply as the bulk of

116. It would be helpful if at this stage some simple analysis of the theoretical implications of the problem were studied by the reader ; see for instance, Benham—Economics, Ch. XXXIII,

the economy operates through banks. What does "Currency" signify in India? The components of currency with the public i.e., column 2 are:

(i) Notes in circulation,

(ii) Circulation of rupee coin,

(iii) Balances of Central and State Governments held at Treasuries, and,

(iv) Cash on hand with scheduled and reporting non-scheduled and State Cooperative banks.

Thus Column 2=(i)+(ii)—(iii)—(iv) as for instance for 1950—51. The calculations would be as follows[117]:

(i)	.........1,238·60	(Rs. Crores)
+(ii)	.... 135·68	,,
—(iii)	.... 4·42	,,
—(iv)	.... 39·10	,,
=Col. 2	.... 1,330·76	,,

Deposit money with the public, i.e., column 3 is a relatively simple concept and is made up of the following two items, *viz*,

(i) Net demand liabilities of scheduled and reporting non-scheduled and State Cooperative banks,

+(ii) "Other deposit" with Reserve Bank of India. However, (ii) is really a very insignificant amount and the total Deposit money with the public i.e., Col. 3, is largely the result of (i). This may be illustrated for 1950-51 as follows[118]:

(i)	.... 614·29	(Rs. Crores)
+(ii)	.... 26·01	,,
=Col. 3	.... 640·30	,,

3·3 *Factors Determining Variations of Money Supply.* As the total money supply of the public shows large variations from year to year it is necessary to enquire into the various factors which account for them. The main influences at work are.:

(a) Government borrowing from the banking system,

(b) borrowing of the private sector from the banking system and,

(c) changes in the foreign assets held by the Reserve Bank of India.

117 For details relating to other years, See Report on Currency and Finance, 1960-61, Statement 21

118 See reference 117.

It is an elementary proposition of public finance that government's total receipts may be, not only at a given point of time but also during a specified period of time, less than its expenditure. If it is not possible for Government to curtail its expenditure, the "deficit" must be financed by borrowing and this leads to what is known as the creation of creidit (which is, in effect, money) by the banking system including the Reserve Bank of India. Thus deficit financing* leads to the creation of additional purchasing power. This enables Government to draw upon the available "real" resources to a larger extent than it could have done if its expenditure had to be confined to its available receipts. It is often argued that such deficit financing contributes to rising prices as it increases the competition for the available scarce real resources.

So far as (b) is concerned, the position is simple. It is apparent that the private sector i.e. individuals and business organisations must borrow from banks, and this must add to money supply, if their current expenditure is in excess of their current income. This would also contribute to a rising trend of prices like deficit financing, the difference being that an increase in Government indebtedness to the banking system is usually of a far larger amount than that of private indebtedness to the banks, and what is more significant is that Government could more or less "compulsorily" borrow from the Reserve Bank of India and thereby use its supreme powers to bring about induced inflation, a phenomenon often cryptically referred to as the use of the printing press for raising resources[119]. Finally, there is the net adverse balance of payments which reduces the foreign assets held by the Reserve Bank of India. Theoretically, there could be a net favourable balance which would increase our foreign asset holding, but under present conditions one might as well ignore such a possibility. It is clear that if we have a net deficit in our international payments relations *vis-a-vis* the rest of the world, we must meet it either by external assistance or running down our foreign balances, particularly our sterling balances. The process is somewhat as follows—exports being less than imports, the tendering of foreign exchange for conversion into rupees would be less than presentation of rupees for obtaining foreign exchange to

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* For deficit financing as a plan resource in India, see Vol. I pp. 452-454.

119 See Dalton—Public Finance, Ch. XV.

make payments abroad. In other words, if imports exceed exports and there is a net adverse balance of payments rupees would flow into the Reserve Bank who would pay out foreign-exchange. This would have the effect of reducing the circulation of rupees in India and decreasing the money supply with the public—opposite results taking place when there is a net favourable balance of payments for India.

We, therefore, find the paradoxical position that an expanding developmental economy would have contradictory forces operating simultaneously on the money supply with the public. On the one hand, expanding expenditure would lead to deficit financing which has the effect of increasing money supply with the public; on the other hand, an inevitable adverse balance of payments may, if there is no other way of financing the excess, lead to a contraction of money supply with the public. However, if the adverse balance of payments could be met by external assistance rather than by running down our foreign reserves, the countervailing effect on money supply being absent, the impact of Budgetary deficits on net addition to money supply with the public would be greater. Thus, when an overall increase in money supply takes place, it is not necessarily correct to assign it to deficit financing as is usually done in quarters which are prone to devote only superficial consideration to such intricate problems. It could be due to deficit financing; but it could be also due to either an increase in the private sector's indebtedness to banks or it could be due to our having a surplus on our foreign account. Again, to put it the other way round, a given volume of deficit financing would lead to a larger net expansion of money supply if during the same period a given quantum of deficit in foreign payments is met by external assistance rather than by running down our foreign balances. Thus it is difficult to correlate any given volume of Budgetary deficit and a given quantum of deficit in foreign payments to any specific rise in money supply unless we probe deeper and look into the method through which the foreign deficit was met. This may be illustrated by what happened during the Second Five Year Plan. We had during the first two years of the Second Plan both budgetary deficits and an adverse balance of payment. The foreign deficits were met by running down our sterling balances; thus, the net rise in money supply was restricted for the budgetary deficits, though large, were countered in their effect on the money supply by the decline in sterling balances. In the third and fourth years of the Second Plan, we continued to have the same phenomenon of budgetary deficits and adverse balance

of payments. During these years, however, we were able to meet our balance of payments deficits by external assistance rather than by drawing on our sterling balances, so that the budgetary deficits had greater impact on money supply and led to a larger increase in it. Finally, it would be wisdom to remember that all increases in money supply do not necessarilly have an inflationary effect. It is quite possible—and, perhaps this is what actually happened in India during the Second Five Year Plan—that an increase in money supply may coincide with an increasing monetisation of the economy (i.e., a decline in the self-consumed portion of the national product through an inerease in the marketed surplus)[120] and in consequence, have a lower inflationary effect for the increased money supply may be required to deal with the increased monetisation of the economy.

3·4 *Variations in Money Supply—the Facts.*—We have discussed above, more or less in abstract terms, the theoretical considerations that lie behind money supply and its variations. Broadly, the conclusions that emerge are:

(a) an expanding economy sets in motion forces that generally tend to increase Money supply with the public;

(b) a deficit in Government account, which is characteristic of large scale planning for development, exerts a pressure towards an increase of Money Supply;

(c) deficit financing, by itself, need not necessarilly be inflationary;

(d) the effect of a deficit in the balance of payments on Money Supply depends on the manner in which it is met, rather than on its volume, and,

(e) all increases of Money Supply need not lead to rise of prices especially in an economy where a trend towards increasing monetisation* is noticeable.

We might now look at the facts and try to undertand what exactly happened during (say) the last three years when the net addition to Money Supply with the public was substantial (see para 3·2). The following table gives the details of the factual information:—

120. See article on Marketable Surplus by Shyam Nandan Sinha in A.I.C.C. Economic Review April 7, 1962; compare also Vol. I, pp 204-05.

* This phrase includes both a decline in self-consumption and a shift from barter to the money 'nexus'.

TABLE for para 3·4

Factors Responsible for Variations in Money supply

(Rs. crores)

	1961	1960	1959
I. Increase (+) in Government Indebtedness to the banking System.	+92·3	+ 24·4	+247·3
1. Increase(+) in Government Indebtedness to the R.B.I.	+146·0	+175·4	+ 95·1
(a) Decline (+) in Government balances with R. B. I.	(—2·4)	(+3·6)	(—10·3)
(b) Increase (+) in R.B.I. holdings of Government Securities	(+130·9)	(+133·2)	(+102·5)
(c) Increase (+) in loans and advances granted to Government by R. B. I.	(+19.2)	(+22·0)	(—4·6)
(d) Increase (+) in Treasury Bills discounted by R.B.I.	(—1·7)	(+16·6)	(+7 5)
2. Increase (+) in Government securities held by banks	—53·7	—151·0	+152·2
II. Increase (+) in Private Indebtedness to Banks	+106·0	+235·7	—107·2
1. Increase (+) in bank credit	+137·4	+243·4	+128·8
2. Decrease (+) in time liabilities of banks	—31·4	—7·7	—236·0
III. Increase (+) in Foreign Assets held by R.B.I.	—59·7	—26·9	+24·3
IV. Expansionary (+) impact of changes in other assets and liabilities of R.B.I. and other banks	+1·9	—17·1	+7·0
V. Recorded Increase (+) in Money Supply	+140·5	+216·1	+171·4

Source : Ministry of Finance.

An important clarification with regard to the above should be emphasised. It has been pointed[121] out that:

121. Ministry of Finance, Economic Survey 1961-62, issued on 14th March 1962 with Budget Papers.

The analysis in the above table is in terms of recorded changes in the balance-sheets of banks and the Reserve Bank. These changes include variations in the PL 480 counterpart funds which were lodged mainly as time deposits with the State Bank upto May 12, 1960. According to the new procedure adopted since then, these funds flow directly to Government through purchase of special securities by the U.S. Embassy and as such have no effect on the assets and liabilities of the banking system. However, during the 12-month period July 1960 to June 1961, part of the past accumulation of PL 480 funds with the State Bank were also transferred to Government in monthly instalments of Rs. 12 crores each. For monetary analysis the counterpart funds may be treated as Government deposits rather than private deposits. Upto 1959, there was a net increase in the PL 480 deposits held by the State Bank of India ; hence the figures given above tended to overstate Government indebtedness and to understate private indebtedness to the banking system. The reverse was the case in 1960 and 1961 when there was a net decline in the PL 480 funds held by the State Bank of India."

It may, further, be pointed out that item III of the table is exclusive of International Monetary Fund transactions, and excludes for 1960 repayment of Rs. 34·5 crores to I.M.F. and for 1961 the net loans receipt of Rs. 58·3 crores from I. M. F.

Analysis of the table seems to suggest that in 1959 and 1960, there was a trend towards an accelerated increase in Money Supply. This, however, appears to have been halted, perhaps even reversed, in 1961. The increase in Money Supply with the public was as follows :

1959 ... ... 7·3 per cent
1960 ... ... 8·6 per cent
1961 ... ... 5·1 per cent

The two major factors which seem to have been operating for slowing down the rate of increase in Money Supply were :

(a) a slower pace of increase of bank credit to the private sector, and
(b) a somewhat larger decline in the foreign assets held by the Reserve Bank in 1961 than in the preceding two years.

It seems that these two factors led to a smaller increase in Money Supply in 1961 despite a larger increase in government's indebtedness to the banking system than in 1960.

4. India's Foreign Reserves.

4.1 We have seen that there was a somewhat larger decline in the foreign assets held by the Reserve Bank of India in 1961 than in 1960. It would be useful to analyse the trends of our foreign reserves as these constitute, in a sense, our basic line of defence for meeting the adverse balance of payments which must continue to be a feature of the Indian economy for sometime to come. The following table indicates the position :

India's Foreign Exchange Reserve

(Lakhs of Rupees)

End of Year	Assets	Movement (Increase + Decrease —)
(1)	(2)	(3)
1950-51	951,41	+ 28,55
1955-56	824,61	+ 10,47
1956-57	681,10	—143,51
1957-58	421,22	—259,88
1958-59	378,92	— 42,30
1959-60	362,87	— 16,05
1960-61	303,61	— 59,26
July 1961	260,03	(lowest in 1961)
Dec. 1961	316,74	+ 5,72 over Nov. 1961
Jan. 1962	304,02	— 12,72
Feb. 1962	302.35	— 1,67

Source : Reserve Bank of India.

It is obvious that our external payments position is extremely unsatisfactory. The position showed a distinct deterioration during the year in spite of a substantial increase in foreign assistance and led to a decline in our foreign exchange reserves by Rs. 59 crores in 1960-61 as compared to a decline of Rs. 16 crores in 1959-60. In July 1961, the reserves touched the lowest level and, though there was a slight improvement and it rose for sometime, a steady decrease is again noticeable in the first two months of 1962.

4·2 The low (and declining) level of foreign exchange reserves were naturally a source of considerable concern. To

this were added during the last few years a rapid decline in receipts from "invisibles" and a large increase in payments for imports. India, therefore, had to negotiate in 1960-61 for a much larger volume of assistance than she required in the previous year. A total authorisation of Rs. 970 crores was secured in 1960-61 under loans and P.L. 480 credits, the amount being higher by over Rs. 500 crores as compared to 1959-60. Grants during 1960-61 accounted for Rs. 34 crores.

4·3 An interesting feature of our plan financing has been the continuous inroads that we have been making on our sterling balances. These balances touched an all-time peak record of Rs. 1732·56 crores on April 5, 1946. Some of it was used during 1946-47 till the partition of the country split the balances, and on April 2, 1948 (i.e., the beginning of the first financial year after Independence) our sterling balances stood at Rs. 1543·94 crores. At the beginning of the First Five Year Plan, it was further reduced and stood at Rs. 875·17 crores. Between 1951 and 1956, these balances were further heavily drawn upon and it stood at Rs. 748·51 crores on April 6, 1956. The Second Plan period made further demands on it and by the end of the Second Plan it had been reduced to less than Rs. 200 crores. One is, therefore, compelled to the conclusion that we have been more or less living on our sterling balances, and, in view of the part it has played during the last decade one can only look back with wonder at all the criticisms that were levelled against its acquisition upto 1947.

5. Developments in Exchange Control.

5·1 *Origin.* During and after the Second World War few countries were left in a happy position as regards their balance of payments. Persistently adverse balance of payments has prompted many countries to adopt the device of exchange control to combat the difficulties of a chronic deficit in the country's balance of payments. India has been no exception to this almost universal trend.

5·2 *Concept.* Exchange control is a method of preventing a deficit and is adopted by weak currencies with the purpose of maintaining, at least nominally, an exchange value for its currency at a level higher than what it would have secured in a free market. The artificialy higher foreign value given to the country's currency *ipso facto* implies pricing some foreign currencies at a rate lower than they would be under conditions of a free market; this must logically lead to the rationing of such currencies, and, exchange control is the mechanism for such rationing.

5·3 *Significance of Exchange Control*. What, it might be asked, is the significance of the rupee being subjected to exchage control? Since, in view of the exchange control, the rupee is not freely convertible into foreign exchange, it is not possible for individuals and firms to get as much foreign exchange as they desire. All allotments of foreign exchange are made by the Reserve Bank of India which naturally strictly regulates the amounts made available to each applicant and ensures that they are given only for approved purposes. Exchange control, being a feature generally of conditions of trade deficits, is usually accompanied by vigorous export promotion measures. Paradoxically, however, in spite of export promotion, exporters can hardly be allowed, under conditions of exchange control, to retain the foreign exchange they acquire or even to use it in any manner they wish. Thus, exchange control inevitably implies compulsory surrender of foreign exchange earned to the central bank of the country at, of course, the official rate. Since such a policy might nullify attempts at export promotion, steps are sometimes taken to enable the exporter to get at least a part of his foreign exchange earnings as a matter of right automatically. This method is commonly known as "currency retention" and has been adopted in several countries with a fair degree of success. The purpose of currency retention is to make possible, as an economic proposition, induced exports contrary to conditions of comparative advantage and relative levels of prices at home and abroad. The inducement is made effective through currency retention in the following ways:

(a) enabling imports for development of export industries, and

(b) recouping of losses (or compensating for artificially reduced profits) by enabling imports of such items as can be sold profitably in the home market.

5·4 *Exchange Control and Export Promotion*. Indian exporters have been persistently claiming that a prescribed percentage of their export earnings should be permitted to be held by them under the provisions of a currency retention scheme. While some of the exporters would undoubtedly prefer a complete freedom* in the matter of utilisation of the foreign exchange allowed to be retained by them, the more progressive of the exporters recognise that some restrictions on the types of imports permitted seen unavoidable. This aspect of the question was carefully examined by the Import

*One exporter is reported to have offered to export at a loss of even 50% if for every 1 Lakh Rupee worth of exports he is allowed to import a Cadillac car. !

and Export Policy Committee, 1962, who, however, were not favourably disposed towards the scheme of currency retention. They observed :

> "In our opinion it is, however, not necessary to let the Indian exporters have a free hold on any percentage of their export earnings. Instead the scope of the present 'Export Promotion Schemes' should be widenend to cover all exports. The exporter's choice to import should not be limited to one or two items as is the case at present. Indeed, the import licence issued to exporters and manufacturers under this arrangement should be permitted to be used for any raw materials, components or equipment which the exporter or manufacturer may care to import for the manufacture of the 'export-product' except such items as have been specifically banned by public notice or notified in the license. ....If the imported commodities are not required for a particular industry, they may be allowed to be sold to a sister industry."[122]

It is difficult to share the opposition of the Committee on Import and Export Policy in this respect. Exchange control, like all controls, involve restrictions on freedom of economic action. Without being an advocate of the old *laissez faire* economy, one could reasonably plead for reductions on restrictions, provided such freedom did not endanger national planning policies. In fact, one could go further, and argue that to the extent effective export stimulus must depend on the private sector's efforts, it is only proper that the freedom and initiative of that sector should be allowed to have a freer scope within the general framework of policy control. It seems, therefore, that on the whole a net national advantage could follow from the adoption of a policy of "currency retention" with clear and specified categories of prohibited imports for which the retained foreign exchange could not be used.

5·5 *Recent Developments in Exchange Control.* The continuously rising deficit in India's balance of payments has led to progressively tighter measures of exchange control being adopted during the last three years. Some of the more significant of these measures[123] are summed up below :

1958-59 : (1) The free limit of Indian and foreign currency notes that could be taken out of India by

122. Report of the Import and Export Policy Committee, 1962, p. 34.
123. Extracted from the various issues of the Reserve Bank's Reports on Currency and Finance.

travellers was reduced from Rs. 270 to Rs. 75.

(2) In view of the active participation of Indian Banks in financing the country's foreign trade and their considerable expansion of foreign exchange business, a composite association was formed, viz., the Foreign Exchange Dealer's Association of India, comprising of all authorized dealers.

(3) A "Bilateral Account" group was formed whereby for U. S. S. R., the German Democratic Republic and Poland, all payments for imports from and exports to, these countries could be settled only in rupees.

1959-60 : (4) It was provided that all trade with Egypt could be invoiced only in Indian rupees, and proceeds of Egyptian cotton imports were to be utilised for payment for exports to Egypt of tea, jute goods and other specified commodities.

(5) The "Bilateral Account" group [i.e., (3) above] was extended to include also Bulgaria, Czechoslovakia, Hungary, Rumania and Yugoslavia. It was provided that all financial transactions between India and countries covered by the bilateral trade agreements would be conducted on a non-convertible rupee basis. It has further been laid down that rupee balances held by banks in these countries would not be transferable to any other country or convertible into any foreign currency.

(6) A "Limited Payments Agreement" was concluded with Pakistan to cover on a non-convertible rupee basis payments for trade in a few specified commodities with specific monetary ceilings.

(7) A tightening up of capital remittances abroad was undertaken by reducing the limit of sums transferable on emigration by Indian nationals. The earlier limits were, per family unit,

Rs. 75,000 for dollar areas
Rs. 125,000 for non-dollar and non-sterling areas, and,
Rs. 200,000 for sterling area.

These were all fixed at Rs. 50,000, thereby also removing the discriminating feature in controls on export of resident capital.

1960 61 ; (8) Notifications were issued prohibiting taking out or bringing in of Indian bank notes of Rs. 100 or higher denominations.

(9) Minor restrictions were imposed regarding foreign exchange to students taking up non-technical courses abroad.

(10) It was felt that exchange should not be made available for pleasure travel, and so instructions were issued prohibiting booking of passages in case of conducted tours for pleasure travel to foreign countries even if the cost of such passage was within the prescribed limits.

During the last three years certain minor relexations have also been introduced, especially with a view to rationalisation and adjustment to changes in regulations in foreign countries. The general trend, however, has been towards stricter control in order to

(i) meet the situation arising from a move by several countries abroad in the direction of full convertibility of their currencies,

(ii) remove loopholes in existing regulations,

(iii) conserve available foreign exchange, and

(iv) encourage the inflow of capital.

5 6 *Economic Effects of Exchange Control.* The primary effect of exchange control, like all controls, is to encourage evasion, since the demand for foreign exchange would exceed the supply as the shortage of availability of foreign exchange is the incentive for introducing exchange control. Collusive evasion becomes possible if exporters and importers could arrange with their counterparts in foreign countries to invoice fictitious values to goods moving over or coming in. Normally, however, one does not expect reputable firms to engage in such practices ; but, even then, strict watch has to be kept on export prices and import prices as otherwise it may be possible for

(a) exporters to acquire foreign balances by invoicing their exports below their value, and,

(b) importers to retain foreign exchange by having their imports invoiced at more than their supplier's costs.

Heavy penalties are imposed on violations of exchange control orders and perhaps the worst effects of such control are the irritations caused to honest parties. Further, exchange control leads to meticulous and detailed control on foreign trade by Government. Government, for instance,

I.B.R.D. Loans *vis a vis* Total External Assistance

(Rupees crores)

		I. B. R. D.	Total
1.	Aid authorised upto the end of First Plan	... 57·7	420·5
2.	Aid utilised upto the end of First Plan	... 33·8	227·9
3.	Aid undisbursed at the end of First Plan (1—2)	... 23 9	192·6
4.	Aid authorised during the Second Plan	... 265·3	2568·8
5.	Total available aid after 31st March, 1956 (3+4)	... 289·2	2761·4
6.	Estimated utilisation during Second Plan	... 222·6	1466·5
7.	Undisbursed Aid as on 31st March, 1961 (5—6)	... 66 6	1295·4

Source : Reserve Bank of India

N. B. Total figures include P. L. 480 Aid.

The requirements of external assistance during the third plan period are estimated to be Rs. 2,600 crores. In arriving at this estimate P. L. 480 imports have been excluded. The consortium meetings organised by the World Bank in May and June 1961 has enabled a provisional commitment of assistance of the order of Rs. 1,100 crores so far, out of which I. B. R. D. and I. D. A. assurances for 1961-62 being Rs. 125 crores and for 1962-63 Rs. 75 crores, in round figures.*

7. Indian Monetary Policy.

7·1 *Role of Monetary Policy.* The objectives of monetary policy could cause as much differences of opinion amongst economists as political ideology could amongst politicians. The traditional controversy between external stability and internal stability is now a dead issue; and, so is the battle between advocates of stability of prices *vis a vis* the exponents of rising (or falling) prices. The emergence of planning as a tool for economic development has subordinated questions relating to the independent objectives of a monetary policy,

*Report on currency and finance 1960-61, p. 110.

for it is increasingly being recognised that monetary policy is only a tool for planning, and is to be utilised for furthering the objectives of planning. It is necessary, however, to bear in mind that Planning is not an end in itself (a point which planners all over the world, particularly in underdeveloped countries, very often fail to realise) but that it itself is only a means to the achievement of greater welfare.* It is true that no universally acceptable norm for greater welfare could be easily formulated, though there would perhaps be a large measure of acceptance to the proposition that raising the *per capita* national income (consistently with a more equal distribution of the aggregete national income) together with reductions in involuntary unemployment constitutes the ultimate ideal of economic development. In the context of such objectives of planned economic development, the role of monetary policy is obviously rather limited as total planning can no longer rely on the indirect mechanism through which monetary policy must perforce operate. The necessity and importance of establishing central control in matters which were previously left to be achieved through individual initiative is being increasingly recognised and universally accepted. This has led many to believe in a continuous extension of the public sector, a belief, which like planning, is threatening to become an end in itself, instead of remaining what it was intended to be, *viz.*, a means to promote economic development. We, in India, have adopted and given to ourselves a constitution that is intended to achieve equitable distribution of the benefits of progress and independence, and, have asserted[125] that

> "In the last analysis, economic development is but a means to an end—the building up, through effort and sacrifice widely shared, of a society, without caste, class or privilege, which offers to every section of the community and to all parts of the country the fullest opportunity to grow and to contribute to the national well-being."

In the context of India's planned economic development, monetary policy in the traditional sense of the term has lost much of its significance, even with the widening of the concept of monetary policy to include not only the policies of the Reserve Bank of India but also the policies of Government relating to import control, public debt management, taxation and pricing of products of State Undertakings. Nearly 25 years ago, J.M. Keynes, the apostle of revolutionary monetary theory pointed out, in the context of a decision

*See Vol. I, pp. 1—6 and 445-47.
125 Third Five Year Plan, pp. 18-19.

on what scale and by what means it was right and reasonable to call on the living generation to restrict their consumption (in other words, to induce a higher rate of savings), so as to achieve a higher level of development by establishing a state of full investment, in course of time, for later generations, the rather limited role that monetary policy could be expected to play. Keynes[126], almost prophetically, stated :

> "The State will have to exercise a guiding influence on the propensity to consume partly through its scheme of taxation, partly by fixing the rate of interest, and partly, perhaps, in other ways. Furthermore, it seems unlikely that the influence of banking policy on the rate of interest will be sufficient by itself to determine an optimum rate of investment I conceive, therefore, that a somewhat comprehensive socialisation of investment will prove the only means of securing an approximation to full employment; though this need not exclude all manner of compromises and of devices by which public authority will co-operate with private initiative."

We have proceeded far beyond what Keynes contemplated in the field of State Socialism which to-day embraces a large part of our economic life. The State has to-day assumed, not only large scale ownership of the instruments of production but also, wide powers to determine the aggregate amount of resources to augment the instruments of production, their occupational and regional allocation, and even the rewards to be obtained for their use when they are owned privately. Under such conditions, and in the context of a declared goal to achieve a socialistic pattern of economy, it would be futile to expect that monetary policy as such could achieve any significant results towards promoting the objectives of Indian Planning.

7·2 *Scope of Monetary Policy.* It has been argued above that under present conditions monetary policy cannot be expected to accomplish much. Its limitations are being increasingly recognised even in the developed countries, while its scope in a developing economy is still less. The limited scope, however, does not mean that it has no part in the sum total of the armoury of economic intervention; though subservient to the requirements of economic growth, monetary policy can through suitable application of mone-

126. The General Theory of Employment, Interest and Money, p. 378.

tary instruments, make Government's planning policy more effective. In other words, a developing economy can be aided to run more smoothly if monetary and fiscal policies are properly co-ordinated with a view to speeding up the pace of economic growth. The Reserve Bank of India* apparently had something of this sort in mind when it stated :

> "Monetary policy, despite its recognised limitations generally and especially in a semi-developed economy like ours with a substantial currency component of money supply, has a positive role to play in facilitating the attainment of growth with stability. The techniques of credit regulation, however, have to be modified to suit the changing outlook of the economic scene, bearing in mind the needs of a developing economy."

We may, in the context of the above policy statement, examine two issues, *viz.* :

(a) factors limiting the efficacy of monetary policy,

(b) the specific objective of monetary policy in a planned economy.

7·3 *Limiting Factors of Monetary Policy.* If monetary policy is to play any part there must be a money economy. A large production sector that operates without the stimulus of a price mechanism hardly provides a satisfactory base for an efficient monetary policy. Again, an economy in which the State is the major investor in new activity and regulator of investment activity in the private sector is obviously an economy in which the importance of monetary policy is circumscribed. In short, since monetary policy must work itself through the price mechanism, anything that obstructs the functioning of a market economy must restrict the usefulness of monetary policy, and, the Indian economy in the last decade has been typically an economy of an underdeveloped country where monetary policy could not possibly achieve results that it could be expected to achieve in U.K. or U.S.A. India, however, has been changing rapidly. The production sector outside the orbit of monetary transactions is steadily decreasing ; a growing importance of bankmoney is noticeable ; development of an organised and integrated money and capital markets is taking place ; the role of the banking system in mobilising savings and financing of trade is on the rise ; in short, the pace and pattern of our economic growth is making possible conditions wherein monetary policy could be more effective. At the same time, the emergence of planning and the technique of direct intervention

* Annual Report 1960.

by the State in the realm of economic life must tend to make the price-mechanism and the free market of less significance, making monetary policy recede to the background.

7·4 *Objectives of Monetary Policy Under Planning.* A period of intense planning for securing rapid economic growth requires for its success a certain measure of stability in the value of money—internal as well as external Investment calculations are apt to be upset if the prices of investment goods rise rapidly or violently. Again, a rising price-level imposes a restraint on savings and capital formation since a larger slice of income goes to meet consumption needs, especially where, as in India, rising *per capita* income coincides with a period of raising of levels of living.* A developing economy needs, in the early stages, a large import-surplus that creates a balance of payments deficit and strains the stability of the external value of the currency, requiring intensive exchange-control measures. Thus the objective of rapid growth requires the adoption of policies which assume a certain measure of stability in the internal and external value of money, towards the achieving of which monetary policy must be directed.

7·5 *Reserve Bank of India and Instruments of Monetary Policy.*—The traditional weapons of monetary regulation were the Bank-Rate and the Open Market Operations. To this, Keynesian monetary theory added the power to vary the reserve-ratios of member banks. The Reserve Bank of India has at its command today practically a text-book like perfect set of powers, which, *inter alia*, include the following:—

(a) Bank rate,

(b) Open Market Operations,

(c) power to introduce variable reserve ratios,

(d) power of selective credit control,

(e) powers of regulation and supervision of individual banks,

(f) powers to acquire a wide range of assets, and

(g) control over the bill market.

The decade 1951 61 is a decade of great and significant changes in the country. It is also the first decade where India as an independent country sought to use all the instruments at its command for promoting welfare of its people. Statutorily, and in theory, the Reserve Bank of India undoubtedly has a large measure of independence. It would,

*See Vol. I, Ch. III.

however, be better to frankly recognise at the very outset that the Reserve Bank of India, though a quasi-independent organisation, is essentially and in ultimate analysis an organ of the Government of India. To say that the Reserve Bank's policy of regulation of the credit system must perforce reflect the decisions and thinking of the Government of India is not, of course, to imply that the Reserve Bank can do nothing without governmental approval. The Bank has a large positive role to play in building up (as distinguished from regulating) an adequate and efficient credit system to cater to the needs of a growing economy. In this field of promotional aspects of central banking, the Reserve Bank of India is undoubtedly capable of much independent action, though even here it must, by and large, tow the line laid down in schemes of planned economic development. Further, the dependence of the Bank to governmental fiats has been particularly great since the beginning of the Second Five Year Plan because the Bank's monetary policy had to follow, and be determined by, the economic trends in the country which were being increasingly determined by government's overall planning policy.

8. Review of the Reserve Bank's Monetary Policy.

8·1 *The General Background.* In 1950-51 there was a substantial monetary expansion and rise in prices due to the Korean war boom. The Reserve Bank, perhaps, inadvertently contributed to the expansionist tendency by its large purchase of government securities—a policy that added to inflation when the Bank should have probably adopted a policy of credit restraint. In 1951-52, with the end of the Korean war, there was contraction of money supply and a sharp fall in commodity prices. The Reserve Bank suddenly woke up to its responsibility as the head of the monetary system and announced in November, 1951 measures of monetary restraint. Apparently the measures were intended as anticipatory action, though it is difficult to say at this stage what evidence was available to conclude that an abnormal rise of bank credit of the magnitude witnessed in 1950-51 would recur. One is tempted to regard the measures of November 1951 as perhaps mere exercises of a newfound realisation of powers. The three years 1952-55 were fairly smooth with prices remaining fairly stable—in fact, showing a fall with the good agricultural production of 1954-55. The activities of the First Five Year Plan were not only rather restricted but the tempo of investment in the country had not yet been properly stimulated. 1955-56, however, marked the beginning of change. There was a marked rise in the rate of investment

in the country while both deficit financing and private sector's indebtedness to banks rose sharply. Commodity prices depicted an upward swing along with an expansion of money supply. Balance of payments difficulties were visible, and but for the large deficit in our international payments position, monetary expansion might have been faster. The Reserve Bank adopted some credit restraint measures, but since circumstances were no longer as favourable to it as they were in 1951, the success of the measures were extremely limited. In fact, the Reserve Bank failed to fulfil the expectations that many had and its monetary control policy turned out to be mere 'sound and fury signifying nothing.' The next two years—1957-59 were favourable to the Reserve Bank and it was able to recover some of its prestige in the matter of monetary control, not because its policies were any more scientific or any better thought out but because the mounting foreign exchange difficulty slowed the tempo of investment. Industrial output* also failed to rise at the same rate. The result was that trend of commodity prices showed restraint and the pace of expansion of money supply and bank credit slowed down. The Reserve Bank adopted some selective credit control measures and continued its previous policy of credit restraint. As these two years and 1958-59, which showed a marked decline in budgetary deficit, were on the whole less trying, the Reserve Bank's fair weather monetary management came through without serious challenge. The lack of strength in the Reserve Bank's policy was revealed in 1959-60 when investment and industrial production both again revived. There was a marked rise of commodity prices and for the first time industrial raw materials and manufactures showed significant upward trend. The Reserve Bank was unable to prevent the expansion of money supply and bank credit that followed nor check the large decline in foreign exchange reserve that took place. Strangely enough, the Reserve Bank hesitated to take firm action for general credit restraint, and it was not till the fag end of 1960 that it woke up to the need for such action. Appropriate monetary policy does not involve merely taking action according to text-book norms; its real significance lies in proper timing and judged by this test the Reserve Bank's policy was a dismal failure. Apologists for the Bank, while admitting that the Bank's policy was not always properly timed, attempt to defend the Bank and try to explain away its dismal failure by arguing that

(a) the tenor of Reserve Bank policy has been basically right, and

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* For trends in growth of Industrial Production, See Vol. I, pp. 230-237.

(b) the Bank could not restrict credit in view of the needs of a growing economy and, hence, its function was that of achieving "controlled expansion."

The first explanation is rather puerile and is more a play on words than anything else. One might question the utility or the rightness of a basic tenor of policy, if, in effect, it was unable to achieve at the right time the right degree of quantitative restriction. As regards the second explanation, it must be admitted that proper monetary policy must meet the legitimate requirements of an expanding economy; but, did the Reserve Bank succeed in curbing unproductive and speculative uses of credit? There is little evidence that it did achieve even what it claims to have attempted, nor is there any reason to believe that it could have, for no method has yet been discovered by which speculative activities can be automatically separated from non-speculative activities nor stop the flow of credit to what are called speculative activities. Finally, controlled expansion must mean, if it means anything sensible, that increases in money supply did not outstrip trade demands. Logically, such controlled expansion should lead to no untoward rise of prices. Since official policy was to keep prices down,[127] by implication the rise of prices was admitted by unhealthy. It would, therefore, appear rather paradoxical to claim credit for successful controlled expansion and, at the same time, admit[128] that there was "evidence that monetary factors had contributed to an increase in aggregate demand and thereby to the pressure on prices" and that there was "need for a further reinforcement of official policy to hold the price line, through action on the non-monetary as well as monetary fronts." On the whole, one is compelled to the conclusion that Reserve Bank's monetary policy during the last decade has been half-hearted and halting, being more of the routine administrative type than visionary and imaginative. It has been aptly said[129] that

> "The art of the Management of Money consists partly in devising technical methods by which the central authority can be put in a position to exercise a sensitive control over the rate of investment, which will operate effectively and quickly, and partly in possessing enough knowledge and prognosticating power to enable the teachnical methods to be applied at the right time and in the right degree to produce the effects on prices and earnings which

127. Report on Currency and Finance, 1958-59, p. 20.

128. Report on Currency and Finance, 1959-60, p. 22.

129. Keynes—Treatise on Money, Vol. II, p. 212.

> are desirable in the interests of whatever may be the prescribed ultimate objective of the monetary system which is being managed."

The Reserve Bank of India never even came near to such an attitude, perhaps was not even aware that such alertness was expected of it; its monetary policy during 1951-61 was, in fact, a lesson in slothlike inactivity.

8·2.1 *Bank Rate.* Changes in the Bank-rate as an instrument of controlling the volume and terms of credit, and international movement of capital, is a device known to central banking for more than a century. Variations in Bank-rate are aspects of a policy of monetary management intended to influence the volume and terms of credit through a policy of "dear" (or "cheap") money.* The concept of the Bank rate owes its origin to the Bank of England who regard it as the minimum official rate at which it will lend money on short term by rediscounting approved bills. It is an outcome of the concept of the central bank of a country being "the lender of last resort". In the days of the International Gold Standard and free movement of short-term capital between countries in response to imbalances in interest rates in international financial centres, the Bank rate operated primarily through international movements of gold and capital, and secondarily through effects on internal volume of purchasing power in circulation and enterprise at home. With the development of exchange control and the abandonment of free and automatic convertible currencies, the limitations in the effectiveness of Bank rate policy has increased, and it now generally requires to be supplemented in various ways. Even in U. K. and U. S. A. where the banking system is far more sensitive than in any other country of the world, the response to changes in Bank rate has been slow and unsatisfactory, especially as the business world has often found it difficult to interpret the meaning of a change of Bank rate in any particular instance. One should, therefore, naturally not expect any miraculous efficacy of the Bank rate policy of the Reserve Bank of India for our use of credit is far less than that of cash and our banking system is hardly developed enough to reflect quickly and effectively the induced changes that result from the raising and lowering of the Bank rate. The Reserve Bank of India Act defines (*vide* Section 49) the Bank rate (or, more correctly what is intended to be conveyed by it) as the rate "at which it is prepared to buy or rediscount

*Some elementary knowledge of the *modus operandi* of the Bank Rate would be useful at this stage, see Benham—Economics pp. 448-450;

bills of exchange or other commercial paper eligible for purchase under the Act." The definition really implies that the Act was contemplating a "discount" rate. In India, however, there is hardly any commercial bill market, so that the Reserve Bank has to rely more on the Bank rate being a base for the rate or rates at which it may make advances. In view of the stringent exchange control regulations and practically the non-existence of short-term international capital movement on private account, the Bank rate policy of the Reserve Bank must perforce confine itself mainly for its effects on the domestic economy. Even in this limited sphere, its efficacy was rather limited till the volume of investment activity acquired substantial dimensions as a result of the Five Year Plans. Thus, *prima facie*, one did not expect Bank rate policy to achieve much till about 1957-58 when only did the aggregate volume of investment reach significant levels. However, even after the volume of investment had been stepped up substantially, the efficacy of the Bank rate in India would still be limited because

(a) a substantial and a growing share of investment activity is directly in the public sector, and is specifically under the control of Government who would not, obviously, be influenced much by changes in Bank rate in their investment policy, and

(b) even the private sector investment is subject to direct control of Government through the Industrial (Regulations and Development) Act and measures of control over capital issues.

Calculations of the cost of capital and the cost of building up of inventories, therefore, do not play as great a part in India as they normally do under conditions of free economy, and, this again limits the efficacy of the Bank rate unless changes in it are sharp and variations in it of substantial orders. Strangely, however, we find that the Reserve Bank has been changing it in small degrees when it at all changed its Bank rate, so that it is not surprising that its effectiveness has been fairly low from the point of view of the cost factor during the last decade, while its effect on the capitalisation factor has been practically nil due to continuous capital appreciation through other forces operating on the economy. The history of changes in Bank rate are interesting to study. From November 1935 to November 1951, the Reserve Bank made no changes in the Bank rate, which stood at 3 percent throughout the period. In November 1951 it was raised to 3½ percent. It was like locking the stable door after the

horse has been stolen, for by then the Korean boom was on the decline. In fact, if the Reserve Bank had been really alert, it would have raised the rate at least a year ago when the Korean war boom was rampant ; but, during that time not only did the Reserve Bank not raise its rate, it actually was buying a considerable amount of Government security, thereby adding to the volume of money supply. The only merit that can be claimed for the raising of Bank rate in November 1951 was that it put a formal stamp to the policy of cheap money that permeated Indian policy since 1946. In May 1957, the Bank rate was raised by the Reserve Bank again and it was fixed at 4 percent, at which figure it has remained unchanged since 16-5-1957*. A caution is, however, necessary before we acclaim the Reserve Bank's stability in the matter of Bank rate, for such constancy is apt to give a misleading idea of the position. It is necessary to recognise that in India the significance of the Bank rate lies mainly as a rate on advances. While, therefore, the Bank rate has remained unchanged, the lending rates to scheduled banks have undergone changes. The importance of the distinction between Bank rate and advances rate particularly acquires significance from the end of 1951 when the Bill market scheme was introduced, and, divergence between the Bank rate and the lending rate brought about as a part of a deliberately adopted policy of Reserve Bank's promotional responsibilities. The table given below attempts a study of the discrepancies between the Reserve Bank's different rates :—

	Bank rate	Bill lending rate	Advances rate against Govt. Securities
(1)	(2)	(3)	(4)
Till January 1951	No discrepancy in rates		
November 1951	$3\frac{1}{2}\%$	3%	$3\frac{1}{2}\%$
March 1956	$3\frac{1}{2}\%$	$3\frac{1}{4}\%$	$3\frac{1}{2}\%$
November 1956	$3\frac{1}{2}\%$	$3\frac{1}{2}\%$	$3\frac{1}{2}\%$
February 1957	$3\frac{1}{2}\%$	$3\frac{1}{2}\%$ + Stamp duty of $\frac{1}{2}\%$ *i.e.* 4%	4%

* It is interesting to make a comparative study of the Discount Rates of Central Banks and the time since when they have remained unchanged ; See, Table No. 62 in Reserve Bank of India Bulletin, March, 1962.

(1)	(2)	(3)	(4)
May 1957	4%	4% + Stamp duty of $\frac{1}{5}$% *i.e.* $4\frac{1}{5}$%	

See Table No. 24 Reserve Bank of India Bulletin, March, 1962.

N.B. Unless one reads carefully the footnotes to the table given in the Reserve Bank Bulletin, one is likely to get a misleading impression from the table itself as given there.

From the table given above, certain interesting conclusions follow. It would be seen that for nearly six years *i.e.*, between November 1951 and February 1957, the bill lending rate has been consistently kept lower than the Bank rate, ostensibly with a view to develop the bill market. Equality between the two was re-established in November 1956 ; but, the raising of the stamp duty on usance bills in February, 1957 made the effective borrowing rate against such bills 4%, *i.e.*, higher than the Bank rate. In imposing the higher stamp duty, the Finance Minister had regarded it as "a fiscal measure with a monetary intent." It was obvious that the position that emerged brought about discrimination against borrowing under the bill market scheme, and compelled the Reserve Bank to raise its Bank rate to 4% in May 1957. The raising of the Bank rate by itself would not have removed the discrepancy but the stamp duty was also reduced to $\frac{1}{5}$% so that the divergence was narrowed to an insignificant amount. However, bill borrowing, which had been deliberately given a lower preferential rate for quite some time, now became the costlier form of borrowing and was allowed to remain so presumably because of the greater liquidity of the banks due to the rapid growth of their deposits.

8·2·2 *Graded Lending Rates.* From 1959, an interesting new development was noticeable, *viz.*, a high liquidity of the banking system together with a high level of aggregate monetary demand in the economy and a large volume of bank credit against equity shares. The Reserve Bank felt it necessary to limit the expansion of bank credit by imposing a check on the unlimited access of banks to Reserve Bank credit. Effective from 1st October, 1960, was introduced a system of graded lending rates keeping the Bank rate unchanged. This in reality amounted to the imposition of "penal rates" for borrowing in excess of prescribed quota. What the Reserve Bank did was to fix a quota for each scheduled bank and to charge only the Bank rate for borrowings within the quota, and a graded additional rate for excess borrowing over and above the quota fixed.* As the aim of

* For details of quota etc., Report Finance, 1960-61, p. 42.

the penal rates was to restrict the volume of bank money, the Reserve Bank simultaneously issued directions to all scheduled banks to

(a) adhere to a minimum lending rate of 5% per annum on all advances, existing or new, clean or secured; advances to other banks and co-operative banks and their own employees were, however, exempted from this direction,

(b) raise their average lending rate at least by ½ percent over the base period rate in the year ending June, 1960; exemption from this was granted where the average base period rate was 9% or more, and

(c) limit the interest rate paid on deposits.

These measures, obviously, were effective and led to a substantial decline of scheduled bank credit almost immediately. In fact, there was a slowing down in the rate of deposit growth and an acute stringency in the money market developed, necessitating various measures of relaxation in the Reserve Bank's credit control policy in 1960-61.

8·3 *Open Market Operations.* With the growth of the strength of member banks, a decline in their need for credit from the Central Bank directly through rediscounting facilities usually takes place. This tendency together with the decline in the efficacy of the Bank rate due to developments of exchange control and inconvertible currencies led to the growth of what is known as Open Market Operations* whereby the Central Bank buys or sells securities in the open market with a view to expanding or contracting money supply and volume of bank credit. The early enthusiasm to the efficacy of such operations has declined substantially with the growing recognition that changes in liquidity preference of the public could neutralize to a certain extent the effects of expansion and contraction in money supply. Thus, for instance, if the public holds more cash when the supply of money is increased and less when it is reduced, the buying and selling operations of the Central Bank could, at least to a certain extent, be counteracted. It is, therefore, generally recognised that such operations should be a part of an overall credit control policy and should be adopted along with other reinforcing measures. The Reserve Bank of India is particularly fortunate in having in India a set up specially suitable for conducting Open Market Operations. The Bank itself is free from any restrictions in regard to the holding of

* Some elementary knowledge of the theory behind these operations would be useful at this stage, See Samuelson—Economics, An Introductory Analysis, pp. 319-20.

securities and can deal in Government bonds of any maturity. The Treasury Bill market in India is, unlike U.K. or U.S.A, comparatively unimportant so that these operations involve mainly dealings in Government bonds, of which the Reserve Bank of India has an adequate and diversified portfolio. Finally, the holdings of Government bonds is predominantly by institutional investors, by far the major portion being held by commercial banks, who are particularly responsive to changes in their holdings, especially when brought about by induced action by the Reserve Bank. All these factors, together with the growing volume of net borrowing by Government, makes India a particularly happy ground for effective Open Market Operations. These operations involve in India

(i) buying and selling of foreign exchange by the Reserve Bank, and

(ii) buying and selling securities in the internal market to affect directly the volume of money supply with the public.

The first one is a simple passive operation as the concept of fixed exchange rates imposes on the Reserve Bank an obligation to buy and sell foreign exchange. Exchange control regulations oblige the public and the banks to sell foreign exchange to the Reserve Bank. In any case, with stringent import control, the scope for these operations is rather limited. As regards the second aspect, analysis of the Reserve Bank's activities in this respect seems to suggest that it has so far more or less confined itself to using these operations to meet the seasonal variations in the reserves of the banking system. The Reserve Bank has been buying securities during the busy season and selling them in the slack season. In addition, these operations have been used to facilitate Government borrowing and of maintaining the stability of Government bond prices. It has been, for instance, pointed out that[128]

> "Reflecting the underlying strength of the gilt-edged market, the trend of Reserve Bank's open market operations continued to be one of net sales almost throughout the year. Net sales by the Bank aggregated Rs. 60 crores in 1959-60 as compared to Rs. 89 crores in 1958-59."

In 1960-61, however, there was a reversal, and "during the year the Reserve Bank's open market operations resulted in net purchase of Rs. 125 crores as against net sales of Rs. 60 crores and Rs. 89 crores, respectively, in 1959-60 and 1958-59."[129]

128. **Report on Currency and Finance, 1959-60, p. 43.**
129. **Report on Currency and Finance, 1960-61, p. 55.**

Of course, the entire amount of purchase was not a reversal strictly, for part of it was explainable by the change in arrangements in regard to holding of P.L. 480* counter part funds.

On the whole, the position may be summed up by saying that :

(a) the seasonal aspect of the operations has been, so far, the primary concern of the Reserve Bank, and mitigation of seasonal stringency and counteracting sharp movements of interest rates has been the more important objective in these operations,

(b) facilitating Government floatation of Public Debt and maintaining the stability of Government bond prices has been a significant objective of these operations, though, perhaps, the Reserve Bank has not been very aggressive about this objective till the last three years,

(c) these operations have not been utilised to any significant extent as an instrument of monetary policy, *i.e.*, for influencing the cost and availability of credit.

It is difficult to assess the extent to which fluctuations in seasonal rates of interest [*vide* (a) above] have been avoided or curtailed in view of the large volume of borrowing from the un organised banking system about which data is not fully available. However, some idea of the fluctuations actually existing is illustrated in the table below :

(Per cent. per annum)

(Average of Fridays)	Short-term Money rates: Government of India Treasury Bill rate(2)	Call money rate: Bombay	Call money rate: Calcutta
(1)	(2)	(3)	(4)
1960 October ,,	2 56	4·11	4·37
November ,,	2·57	4·20	4·41
December ,,	2·54	4·18	4·29
1961 January ,,	2·57	5 18	5·15
February ,,	2·60	5·26	5·17
March ,,	2·75	5·26	5·33
April ,,	2·75	5·21	5·26
May ,,	2·75	4·92	4 77
June ,,	2·71	4·46	4·11
July ,,	2·60	3·46	3·34
August ,,	2·40	2·24	2·75
September ,,	2·47	3·87	3·99
October ,,	2·50	4·23	4·42

Source : R. B. I.

* See Vol. I, p. 217, and p. 492

The period October to September covers fairly comprehensively the different busy and slack seasons, and, hence, the table has been constructed accordingly rather than representing the financial year. The Bazaar Bill Rate is very much higher and varies between 11·50 to 13·92 percent per annum.* Even if we ignore the Bazaar Bill Rate, and do not take into account the rate of interest in the unorganised banking sector for which data is not available, the efficacy of the Reserve Bank's policy does not appear to be great as call money rates did vary fairly largely.

The second objective of the policy, *viz.*, maintenance of the stability of Government bond prices has, obviously, been achieved to a great extent as the table below will show :

Index Number of Security Prices (All India)
(Government and Semi-Government Securities)

(Base : 1952-53=100)

	Government of India Loans	State Government Loans	Municipal Port Trust and Improvement Trust Loans	Combined Index
(1)	(2)	(3)	(4)	(5)
1958 Average of weeks	99·2	100·8	98·9	99·4
1959 ,, ,,	100·9	102·4	99·7	101·1
1960 ,, ,,	101·0	102·5	100·0	101·1
1961 ,, ,,	100·9	101·9	99·7	101·0
1962(†) ,, ,,	100·6	101·9	99·2	101·2
1961 January	100·7	101·4	99·7	100·7
February	100·7	101·4	99·7	100·8
March	100·9	101·6	99·7	100·9
April	101·0	101·9	99·7	101·1
May	101·0	101.9	99·7	101·1
June	100·9	102·0	99·7	101·0
July	100·9	102·1	99·7	101·0
August	101·0	102·2	99·7	101·1
September	101·0	102·2	99·6	101·1
October	101·0	102·1	99·4	101·1
November	101·8	102·1	99·3	100·9
December	100·7	101·9	99·2	100·8
1962 January	100·6	101·9	99·2	101·2

Source : Reserve Bank of India.

* Average of available monthly figures during the year,

† See Statement 36 on Money Rates in Report on Currency and Finance, 1960-61.

The Reserve Bank of India through its open market operations, has also engaged, during the last decade, in what are technically called "switch operations." These operations have been undertaken with a view to meeting the maturity requirements of investors. They are intended to ensure a harmonious maturity and yield pattern. The effect of these operations have been to enable the commercial banks to shorten the maturity of their holdings.

8 4 *Variable Cash Reserve Ratios.* In 1930, in his historic book "A Treatise on Money", Keynes[130] argued that

> "..........to provide against the contingency of insufficient ammunition for the carrying on of open market operations *a outrance*, ...the Central Bank should have power to vary within limits the reserve requirements of its member banks."

Five years later, on 1st April, 1935, the Reserve Bank of India was established ; but, the framers of the Act apparently did not have the courage to give to it a power of control that had been recognised as a very powerful weapon. It took another twenty years before the Reserve Bank acquired this power. In october 1956, the Reserve Bank was given the power to vary the minimum cash reserves maintained with it from 2 to 8 percent in respect of time liabilities and 5 to 20 percent in the case of demand liabilities. It was another four years before the Bank actually used it, for it was only in March 1960, that it used the power of varying cash reserve ratios for the first time. Whatever may be the theoretical merits and demerits of the power to vary cash reserve ratios, the caution with which this power has been extended or utilised makes it an unusual, if not a revolutionary, measure. It is necessary, therefore, to understand the background in which the use of this power was considered desirable. It may be emphasised that it was not rise in bank deposits, as such, that necessitated the use of this power. Bank deposits were rising fast from 1957 onwards, but there was reason to believe that the bulk of the increase in deposits was utilised by the banks to acquire Government securities. In 1958-59, however, there was a change in the situation, and, the following features were noticeable from 1958-59 onwards :

(i) the busy season of 1958-59 recorded a sharp increase in bank credit and the contraction in the following slack season was much smaller,

(ii) in 1959-60, there was a sharper rise in bank credit in the busy season,

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130 Keynes—Treatise on Money, Vol. II, p. 372.

(iii) a steep rise in commodity prices took place,

(iv) credit restraint had become difficult due to the marked increase in the liquidity of the banking system, resulting from its substantially increased portfolio of Government securities.

These unusual developments—unusual only in the sense of being not usual, and not in the sense of being sudden—prompted the Reserve Bank to feel that its traditional weapons of credit control would not be sufficient. Justifying the use of "variable cash reserves" as an instrument of general credit restraint, it has been stated [131]

> "This policy was dictated by the further sharp rise in commodity prices and the recognition of a shift in the character of the prevailing inflationary situation ; the upswing in prices in 1959-60 had occurred, unlike in the earlier years, in the wake of an allround increase in production. It appeared that the major inflationary factor was rather the high level of aggregate monetary demand, which needed to be curbed. The boom on the stock exchange contained some unhealthy element and the liquidity of the banking system was also substantial and these required corrective action. The Reserve Bank, therefore, considered it necessary to exercise, for the first time, its power to vary the statutory reserve requirements of the scheduled banks and required them to maintain additional balances equal to 25 percent of the increase in total liabilities since March 11, 1960 ; a further notification was issued on May 5, raising the quantum of additional deposits to be maintained from 25 per cent to 50 per cent, effective May 6, 1960. Selecttive credit controls were extended during the year to cover advances for stock exchange transactions as well as to unsecured loans."

The facts stated are indubitably true. However, the trends were noticeable for sometime past and should not have appeared to the Reserve Bank as something sudden and extraordinary, requiring the use of such unusual measures overnight. Trends such as those pointed out above do not appear suddenly on the horizon ; they should not have looked like "bolt from the blue" to the Reserve Bank of India which has an enormous organization engaged in continuously studying economic and financial trends. If, therefore, its credit con-

131. Report on Currency and Finance. 1959-60 p. 33 ; see also pp. 35-36 for details of the measure.

trol policies adopted earlier from time to time had been properly timed and appropriately enforced, and, if it had adequate and timely knowledge of what was happening in the economy, it would not have been necessary for the Reserve Bank to take up an attitude of being caught with something sudden and unusual. It was not the adoption of the measure that was objectionable ; what was objectionable was the way it was done, the manner in which the country was made to believe that unusual and unanticipated trends forced the hands of the Bank to adopt a measure which, the Reserve Bank should have been aware, would have a sledge-hammer like effect on the banking system and the economy. However, one may ask the question—Did the measure reduce bank credit ? The answer, unfortunately, is in the negative for the banks largely counteracted the effect of the measure by much larger borrowing from the Reserve Bank and smaller purchases of Government Securities. That the banks were able to borrow more from the Reserve Bank[132] was apparently due to its overlooking the fundamental principle of monetary management *viz.* that the various instruments monetary policy have to be used simultaneously and in a coordinated manner to achieve effective results. The R. B. I. kept its lending rate unchanged while adopting the measure of varying the cash reserve ratios with the result that it was an open invitation to the banks to borrow more from the R. B. I. It is true that the banking system also failed to co-operate. There should have been no doubts in the minds of bankers as to the purpose of the Reserve Bank's order, and, normally, a responsible banking system should fall in line with the intentions of the Central Bank, especially where such intentions are in the wider national interest. However, the Reserve Bank had to follow up with measures of graded lending rates to impose a check on bank's unlimited access to Reserve Bank Credit (*vide* para 8·2·2). However, an interesting question that arises is that relating to the exact intention of the Rererve Bank in this respect. No formal statement of policy was issued, but it appears from the subsequent relaxation anounced on 11th November, 1960, that the R.B.I. intended the measure as a temporary one for the slack season, at the beginning of which it was put into force. This is further confirmed by the manner in which the variable cash reserve ratio instrument was applied. It may be pointed out that in imposing the requirements of higher cash reserves, the Reserve Bank applied the ratio

(i) not on the overall liabilities of banks but on the increase in liabilities taking place after 11th March 1960,

132 Report on Currency and Finance, 1960-61, p. 42.

(ii) disregarding the difference between demand and time liabilities, a distinction that was basic to the original conception of minimum cash reserves to be maintained with it.

The basic minimum requirements under the statute provide for a reserve of 2 percent of time liabilities and 5 percent of demand liabilities. The additional reserve requirement was fixed at 25 percent of the increase in total (time plus demand) liabilities and this ratio was enhanced to 50 percent with effect from 6th May 1960 in respect of increases in deposits after that date. It would appear that sufficient recognition was not given to the effect of such measures on the incentive of banks to mobilise savings in the form of deposits, for a 50 percent additional reserve requirement would hardly make any sane banking possible. It is, therefore, not surprising that within six months the R.B I. had to announce relaxations, though its revised measures suggested by innuendo that the system of penalty lending rates announced on 21st September, 1960 would fulfil the R.B.I.'s objective, making unnecessary the continuance of the measures relating to additional reserve requirements in the context of the advent of the busy season and the emergence of acute stringency in the money market. The following detailed extract[133] provides an index to the Reserve Bank's thinking in the matter:

> "Following the September measures scheduled bank credit declined by Rs. 29 crores between September 30 and November 25, 1960 in contrast to a rise of Rs. 3 crores in the corresponding period of the previous year. Also, all scheduled banks raised their lending rates in accordance with the directive and quite a few raised their lending rates by more than half of one percent. It is important to note that while the Bank raised the cost of credit so as to prune down less urgent demands and generally restrain recourse to itself, it placed no restriction on the volume of credit it would make available to scheduled banks. With the advent of the busy season and the emergence of acute stringency in the money market the question of the continuance of the additional reserve requirements had to be reconsidered. Therefore, in conformity with the Bank's policy of operating credit regulation measures in a flexible manner, the Bank withdrew in two stages the directive issued on May 5 regard-

133. Report on Currency and Finance, 1960-61, p. 43

ing the maintenance of additional statutory reserves with the Reserve Bank."

The following measures of relaxation were adopted :

(i) Effective November 11, 1960, further impounding of the increase in liabilities over the level of November 11 was suspended,

(ii) 50% of the reserve already impounded were released through refixing of the additional reserve requirement at 25 percent of the increase between March 11 and November 11,

(iii) the additional reserve requirement was completely revoked with effect from January 13, 1961, and the balance of the reserves impounded released to the banks.

It may be pointed out that the relaxation order took the form of fixation of a reduced ratio with retrospective effect, and, the impounded reserves were "released" rather than "returned", for under the Act, the Reserve Bank cannot specifically return any portion of the impounded reserves.

What did this experiment for the use of variable cash reserves as an instrument of quantitative credit control achieve? We have seen that the measures had little impact on bank credit. It certainly reduced the liquidity of the banking system, but one wonders whether such reduction in liquidity, without a reduction in total bank credit, was intended, or even indirectly desired. Finally, since the impounded reserves were ultimately restored to the banking system, the entire phase of control was like an experiment in temporary dictatorship, during the slack season when the scheduled banks did not mind being frowned at. The Reserve Bank, however, recognised by experience (what it should have realised by pure analysis) that the impounding of cash could be countered by the banks liquidating larger quantities of Government securities—and countered quite safely without loss in capital depreciation because of the Reserve Bank's own policy of maintaining the stability of Government bond prices (*vide* last portion of para 8·3).

One may, therefore, conclude that this phase of the R.B.I.'s credit control policy was a complete failure. It smacked too much like an impetuous child playing with a dangerous toy, luckily for a very brief period.

8·5 *Selective Credit Control.* The powers of selective credit control vests in the Reserve Bank, not under its own statute, but by virtue of the provisions of the Banking

Companies Act, 1949. The measures taken under the selective credit regulations have been made operative in respect of advances against commodities of mass consumption, *viz*, foodgrains, sugar, oilseeds, jute and cloth, which are the items of strategic importance for purposes of such control. The control has also been extended to advances against ordinary shares when, in March 1960, an unhealthy boom was said to have developed.

What are the objectives of such selective credit control? In pure theory, such controls can be used for a variety of discriminatory purposes, like fixation of minimum margins in particular transactions, controlling the level of outstanding advances, correcting regional imbalances in supply and demand of basic consumption goods, meeting the requirements of new branches of banks etc. They can be made both regulatory and promotional, and, one can expect flexibility, adaptability and efficacy from measures adopted by a nation's custodian of monetary prudence, for by definition they are selective and discriminatory as between purposes. The Reserve Bank itself, however, is rather cautious about it, and, maintains[134] that :

> "Selective controls are not designed to correct the general inflationary pressure within the economy nor is their success to be judged precisely by the extent to which the prices of the relevant commodities have fallen; prices are dependent on various factors bearing on the demand and supply position of the commodities. The controls, by arresting an undue expansion of credit in the busy season and accelerating its reduction in the slack season, may be expected to exercise, only a limited, perhaps, a marginal effect on prices, more particularly when banks have large liquid resources."

The above seems to be more an apology than an exposition of purposes and objectives. One naturally does not feel happy when measures of regulation are hedged with qualifications and contain within themselves recognition of counteracting factors, particularly where they are, *ex hypothesis*, selective and dependent on the discretion and judgement of the Central Bank.

Strangely enough the actual measures of selective credit control adopted by the Reserve Bank have been fairly firm and specific, rarely suffering from hesitancy and timidity that one feared would follow from its policy statement of the objectives

134. Reserve Bank's Annual Report, 1958-59.

of such control, or from its contention[135] that "The success of these controls is to be judged in a limited sphere, namely, their impact on the pressure of demand originating from bank credit." The more important of the measures* adopted recently under this group of controls are indicated below :

(1) the directive issued on December 11, 1957 requiring banks to maintain each month an average aggregate level of credit against paddy and rice not exceeding 75 percent of the average of similar advances during the corresponding months of 1955, 1956 and 1957; the percentage for wheat and other foodgrains was, however, fixed at 80; the order was restrictive in its operation in the States of Andhra Pradesh and Madhya Pradesh where the percentage against paddy and rice was not to exceed 60 of the advances in corresponding months of 1957;

(2) on September 10, 1958, a new directive was issued restricting advances against wheat in the State of Punjab to 66⅔ percent of the level in the corresponding month of 1957;

(3) a directive was issued on July 18, 1958, raising the minimum margin requirements for advances against sugar from 35 percent to 45 percent; the order brought within its purview advances to factories in respect of sugar stocks which had been lifted from the factory premises on which excise duty had been paid—other advances to factories were, however, kept free from the margin provision so that manufacturing activity in respect of sugar may not be affected;

(3) on February 9, 1959, a minimum margin of not less than 45 percent of the value of the stocks were directed to be maintained on all credit limits against the security of groundnuts; stocks intended for exports or for use in vanaspati manufacture were exempted to preserve these uses ;

(4) during 1959-60, selective credit controls were extended to cover advances for stock exchange transactions as well as unsecured loans ;

(5) on account of the programme of procurement of foodgrains by some of the State Governments, the directive regulating bank advances against foodgrains was modified to permit a minimum of 25 percent in regard to credit against paddy and

135. Report on Currency and Finance, 1958-59, p. 32.

* Extracted from the annual Reports on Currency and Finance.

rice to purchasing agents of the Government of Orissa and in respect of credit against wheat to storage delivery contractors operating on behalf of the Punjab Government;

(6) in view of the continuing boom on the stock exchange, and with a view to restraining the volume of credit against equity shares, a directive was issued on March 11, 1960, imposing a minimum margin requirement of 50 percent in respect of advances by scheduled banks against equity shares;

(7) relaxation of controls in the case of sugar and foodgrains was undertaken in 1960-61; on February 8, 1961 the provisions of the directive as regards margin requirements in respect of foodgrains were relaxed, reducing the minimum margin requirements from 40 percent to 35 percent; ceiling limits in respect of advances against paddy and rice were increased; the special restrictions imposed in regard to particular States were removed and uniform limits prescribed for the whole country;

(8) restrictions on margin requirements in respect of advances against sugar were first relaxed on December 9, 1960, and subsequently withdrawn completely on April 21, 1961;

(9) on December 12, 1960, it was decided to regulate bank advances against raw jute and jute goods, and, minimum margins and ceiling limits were imposed as follows:

  (a) a minimum margin of 25 percent for advances to jute mills,

  (b) a minimum margin of 40 percent to others on the value of the stocks of raw jute,

  (c) a ceiling limit not exceeding 130 percent with reference to two months periods of 1960;

(10) the restrictions imposed on jute goods was withdrawn by stages on April 24, 1961 and June 23, 1961.

The various measures of selective credit control outlined above broadly indicates that the policy had the following broad features :

(a) they have been mainly applied in respect of advances to trade ;

(b) the following categories of advances have been exempted :

(i) advances to factories,

(ii) credit for movement of goods,

(iii) those intended for export promotion ;

(c) ceilings to credit extension were suitably changed from time to time in the light of production trends.

The general achievement of these measures of selective credit control have been, on the whole, fairly satisfactory. It is true that the very nature of the Indian economy makes it difficult to achieve spectacular results. The extent of bank-financing in foodgrains is very small. Fluctuations in the output of primary commodities are considerable so that wide variations in prices take place from time to time. It is possible to evade these regulations by resort to what are known as clear (*i.e.*, unsecured) advances ; hence, the R.B.I. directed in March, 1960 that the ratio of clear advances to total advances in any month should not exceed the ratio in the corresponding period of 1959. In spite of these factors, the Reserve Bank[136] holds the view that :—

> "The compliance of banks with the selective credit control directives has been generally satisfactory, and banks have found it easier to comply with a directive specifying the permitted order of credit expansion before rather than after such expansion had occurred."

8·6 *A General Evaluation.* Though the Reserve Bank has been in existence for more than a quarter of a century now, its effective role as a guardian of monetary policy to be pursued in the national interest has been confined only to a decade. In a sense, therefore, the experience of monetary policy has not been long enough to permit of precise conclusions. There is, however, no denying that in the context of our planned economy, monetary policy should strive to achieve the object of economic growth with stability. It must encourage a lending policy directed towards achieving increasing production targets and maintaining the optimum level of employment. In regard to the mobilisation of savings, it must bring about an increased rate of domestic savings, encourage international capital inflow and preserve, consistent with the securing of developmental and maintanance imports, the country's foreign balances. Finally, it must guard against an upsurge of inflationary pressures, and yet provide for the continually increasing credit needs of a developing economy. The tasks before the monetary policy are, therefore, complex

136. Report on Currency and Finance, 1960-61, p. 45.

and many-sided, some of which even pull in opposite directions ; and these "cannot be attained except by the constant exercise of knowledge, judgment and authority, by individuals placed in a position of unchallengeable independence with great resources and every technical device at their disposition."[137] One, however, judges the competence of the monetary authority by what it achieves, and not by its statutory authority or by a long list of 'actions' taken. Judged by achievements, the Reserve Bank of India's monetary policy has few claims to be regarded as satisfactory. There has been a more or less continuous rise in the general price-level, which has, of late, shown definite trends towards inflation, possibly induced by monetary forces. It would be futile to derive consolation from an imaginary view that, but for restraining credit control policies, the rise of commodity prices might have been steeper. One does not console a starving man of to-day by reminding him that he did not starve yesterday. Our foreign exchange reserves have been severely depleted, though, perhaps, its using up has been largely a deliberately planned one for purposes of securing investment imports. There is, however, a silver lining behind these dark clouds. The R.B.I's selective credit control policy has undoubtedly achieved a large measure of success. While the average cost of lending by it has been raised, its availability for non-speculative and genuine trade purposes has been, by and large, assured. Its Bank rate policy has been rather passive, and, its Open Market Operations limited to rather minor achievements in the field of stability of Government bond prices. Its solitary exercise in the field of variable cash reserves was a dismal failure. But, the most serious failing of the Reserve Bank in the field of monetary control has been its hopping and hesitant attitude. The R.B.I. appears to have overlooked that measures of credit control cannot produce the required reactions except after an interval of time, and that wisdom in monetary control lies in anticipatory action and not chasing a run-away horse. It is doubtful whether the timing of its actions has been generally appropriate. As Shri H.V.R. Iyenger*, Governor of the Reserve Bank of India once put it :

> "It would by idle for anyone to make the claim—and I do not make it—that the measures taken by the Reserve Bank have at every stage been exactly timed or just appropriate."

137. Report of the Committee on Finance and Industry (1931) para 280.

* Newspaper report of speech in Madras in 1960.

9. Trends of Prices and Pricing Policy.

9·1 *The Background.* In many quarters a serious misconception exists, *viz.*, that economic planning by a state in which industry is to a large extent socialized needs no pricing system. Unless economic totalitarianism is carried to the extreme point of drafted labour, requisitioned capital, assigned allocation in alternative productive occupations and rationed availability of all consumer goods, a price mechanism must determine much of the working of the economy. India has deliberately refrained from totalitarian methods of economic planning, and, therefore, the concept of prices and the price level, even in the traditional sense of these terms, remains important in the economic system, in spite of large and extensive measures of control and direction that have been adopted in the country.

9·2 Price policy as such has been a rather neglected field in India, and received little attention till the eve of the Third Plan. There were good reasons for such complacency. The Second Five Year Plan did not have to face much concern from any steeply rising price-level ;[138] There was, in fact, some recession in food prices. For various reasons, expansion of public expenditure and investment was slower than visualised. There was a general feeling of pushing ahead firmly by mobilising as much resources as possible, even if necessary through deficit financing, though the necessity of regulating inflationary pressures, when they develop was recognised. The beginning of the Third Five Year Plan, however, found us in an entirely changed economic situation. A substantial rise in level of prices had taken place. There are reasons to believe that monetary forces have begun to exert pressure on its upward surge. Indications are not wanting which would justify the conclusion that a public shift from currency to goods is taking place. It is, therefore, not surprising that the Third Five Year Plan recognised that :

> "At the commencement of the Third Plan, the levels of wholesale prices and cost-of-living are already high and it is essential to ensure that there is no accentuation of inflationary pressures in the course of the Third Plan, and that the levels of living of the more vulnerable classes in society are safeguarded."

9·3 There is a more or less universal acceptance of the proposition that it should be a country's objective to increase

138. See Bose, S.K. and others "Consumer Price Trends during Second Plan period"—Monthly Abstract of Statistics, September, 1960.

the power to exercise deliberate control over the price-level; whether the possibilities of such deliberate control are also increasing or not may be more debatable. Growth of knowledge, and a greater armoury of weapons of regulation, leads one to feel that the possibilities of such deliberate control should be greater today than they were in the past; but failure of our monetary policy to achieve any significant success in this respect introduces an element of not unjustified scepticism as to the possible extent of our success in this matter. One's diffidence is further increased by the recognition that a rising trend of prices is, perhaps, inevitable in an expanding economy and that it would hardly be either possible or desirable to curtail the rate of growth to restrict the rise of prices. Planning policy in India is fully aware of this dilemma, as would appear from the following:[139]

> "Certain upward pressure on prices are implicit in development and they have to be accepted. The process of stepping up investment involves creation of money incomes ahead of the availability of goods and services. Investment adds to real national product after a time, and certain types of investment take a longer time to mature than certain others. The larger the investment effort, the greater is the upward pressure on prices. Similarly, the more long-maturing the projects undertaken, the greater is the resultant strain on the system. The substantial transfer of manpower and other resources to new uses involves payment of large monetary rewards. This also is a significant inflationary factor."

It is true that the very process of development releases factors which have a moderating influence, particularly if development implies the utilisation of, as it did in the case of India, resources that were otherwise unemployed. Again an essentially agricultural economy could sometimes raise the level of agricultural production quickly and without large investment of additional capital so as to counter tendencies to a rise of prices of foodgrains and basic raw materials.* It is, therefore, not impossible to achieve economic growth with price stability, though continuous watch is necessary to keep the rise of prices within moderate levels as investment increases, particularly if substantial resources are raised through deficit financing,† because of the gap between investment and saving.

139. Third Five Year Plan, p. 126.

* For relationship between food prices and food production, see Vol. I, Ch. V, para 3.

† For the economic effects of deficit financing, see Vol. I, pp. 452-454.

9·4 *The Concept of the Price-Level.* Rise (or fall) of prices cannot be judged as a whole by looking at individual prices, and the economist's device of the Index Number has to be adopted for watching trends in general movement. In technical language, changes in the purchasing power of money in a given context can be measured only through the quantity of goods and services which a unit of money will command in exchange; in other words, one has to conceive of a sort of a composite commodity, made up of the various individual goods and services in proportions corresponding to their importance as objects of expenditure. An Index Number, constructed to indicate changes in price-level over time, obviously is significant with reference to the base year in terms of which changes are expressed.

9·5 It would, however, be unwise to confine one's attention only to the General Index for all commodities*, which figure, though useful for some broad purposes, does not really convey as much as the movements of group prices, relatively to one another, do. It is clear that so far as problems of internal economy are concerned, it is the movement of group prices which provide the real clue; in terms of broad considerations of forces determining the value of money, particularly for estimating the influence of money supply on it, (*i.e.*, discussions of the so-called Quantity Theory of Money), and for deriving exchange parities between currencies of different countries the overall general series has still some utility. Finally, the important distinction between Index Number of Wholesale Prices and Consumer Price Index Number (commonly known as cost of living index) should be borne in mind. So far as the economic fortunes of particular groups of income-earners are concerned (commonly classified as middle class, working class etc.) it is the sectional price levels relatively to one another, that are important. For a vast country like India, the concept of an All-India cost of living would be as absurd as one for the whole of Europe, or even for the area comprising the European Common Market even if a completely identical currency system, using the same unit of currency, were used. We have to recognise the wide divergencies in living conditions (and ideas relating to living requirements) that exist in the different parts of the country and, therefore, have cost of living indices for particular States, or particular centres.

9·6 *Statistics relating to Prices in India*†. Two impor-

* For method of construction, see Benham—Economics pp. 455-59

† See the Report of the Committee on Revision of Wholesale Price Index Number of which the author had the privilege of being a member.

tant and fairly comprehensive series are published in India. These are

(a) Index Number of Wholesale Prices, and,

(b) Index Number of Consumer Prices (Working Class)

The first one is now published with 1952-53 as base year=100 as a revised series, though corresponding figure for the old series (base August, 1939=100) are published in the form of the new series converted to old base on the formula : 100 of the new series=380·6 being the average for 1952-53 of the old series. Since the essence of the utility of an index number lies in the basis of comparison being a realistic base year, sufficiently close to the years under study so as to ensure a broad measure of similarity in the economic structure and intersectoral price relations, the new series is generally regarded as the more appropriate one.

So far as the cost of living index number (the term index number of consumer prices is, perhaps, technically more accurate) is concerned, we have, at present, regular publication of the index for working class only. The series for middle class has not yet been published.*

9·7 *Trends of General Prices in India—the facts.* It would be useful to note carefully the trends revealed by the official figures regarding movement of wholesale prices. The table given below illustrates the position:—

Index Number of Whole Sale Prices

(Revised series)

(Base : 1952-53=100)

	1951	1956	1958	1959	1960	1961	Jan. 1962
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Food Articles	113·7	99·0	112·0	118·2	120·3	119·5	118·3
(a) Cereals	102·3	92·3	104·7	104·3	105·3	102·0	102·0
(b) Pulses	102·7	78·2	94·0	99·8	92·0	91·0	97 0
(c) Fruit & Vegetable	115·9	108·4	111·9	127·6	121·0	131·0	133·0
(d) Milk & Ghee	104·2	98·8	106·2	112·2	115·8	115 0	114·0

* Some preliminary data relating to this has, however, been published by C.S.O. in Monthly Abstract of Statistics—June 1960 and November, 1961.

(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
(e) Edible Oils	143·3	117·2	123·2	126·9	143·8	158·0	154·0
(f) Fish, Eggs & Meat	101·1	96·6	106·9	110·4	121·1	131·0	139·0
(g) Sugar & Gur	131·0	97·1	122·8	143 0	138·6	121·0	113·0
(h) Others	142·3	124·9	145·7	163·4	168·6	173·0	161·0
2. Liquor and Tobacco	115·7	82·3	93·7	100·7	106·4	103·6	97·3
3. Fuel Power light & lubricant	95·9	101·6	115·2	116·1	119·0	121·8	122·6
4. Industrial Raw materials	147·6	113·2	114·7	119·7	138·8	147·7	137·5
(a) Fibre	112·2	113·9	109·3	110·2	139·3	150·0	126·0
(b) Oil seeds	142·8	114·9	123·6	130·0	144·9	158 0	158 0
(c) Minerals	99 0	99·3	106·9	100·0	97·5	95·0	95 0
(d) Others	128·2	110·1	108·9	117·3	129·2	127·0	129·0
5· Manufactures	118·9	104·9	108·2	109 7	120·8	127 0	126·1
(a) Intermediate products	124·9	110·0	109 4	111·1	127·1	138·4	137·8
(b) Finished Products	117·9	104·1	108·0	109·5	119·8	125·2	124·1
(i) Textiles	130·1	106·1	104·3	104·6	121·2	128·0	124·0
(ii) Metal Products	87·9	128·3	143 1	143 7	147·0	147 0	147·0
(iii) Chemicals	100·9	92·3	103 9	108·2	104·7	109·0	112·0
(iv) Oil cakes	129·9	102·7	128·6	143·7	140·2	146·0	156·0
(v) Machinery and Transport Equipment	89·7	98·1	103·2	105·9	110·7	114·0	116·0
(vi) Others	106·5	99·8	113·2	113·6	115·0	120·0	121·0
All Commodities	120·0	102·6	111·0	115·5	123·0	125·8	123·2

Source : Ministry of Commerce and Industry.

The above table shows that the prices were lower (by about 20%) in 1956 as compared to 1951 indicating that a fall of prices was achieved during the First Plan period. This, however, is misleading and is due to a statistical feature being the result of abnormally high prices in 1951 due to the Korean war boom. However, compared to 1952-53, the fall in 1956 was insignificant, except in the case of foodgrains where the decline was excessive and, probably, harmful, and "could not be arrested in time because there was considerable doubt

for some time as to the appropriate level at which Government ought to buy."[140]

The Second Plan period was characterised by persistent upward trends in prices. Not only did the general level indicated by the all commodities index rise substantially from 102 in 1956 to 126 in 1961, but the more significant feature was the rise in the group index for industrial raw materials and manufactures (both intermediate products and finished products), which rose more steeply than the general index. It may be clarified that foodgrains prices do not reflect in India anymore the full impact of internal production trends due largely to P.L. 480 imports. Leaving aside for the time being the special nature of foodgrains prices, it would not be incorrect to say that the continued upward trend of wholesale prices during the Second Plan period was mostly the result of rising pressure of demand. It is difficult to assess the relative roles of rise in money incomes and growth of population in bringing about this rise, but considering that growth of population in India is a normal phenomenon one would be inclined to regard rising aggregate money supply as the greater villain.

The price situation showed a further deterioration in 1960-61, though it appears to have been arrested slightly. The last two years of the Second Plan were years of a high tempo of investment activity and were marked by continued expansion of money supply and bank credit which obviously were responsible for the uptrend of prices despite the substantial growth in agricultural and industrial production. Thus from the general trend revealed since 1956, one may conclude that price rises have reached dangerous levels, that seeds of an inflationary spiral seem to be germinating, and, the slight recession in January 1962 was perhaps only a passing phase. In fact, during February 1962, the general price-level recorded a fractional rise of 0·2 percent, the Economic Adviser's Weekly general index of wholesale prices (base 1952-53=100) standing at 124·3 for the week ended February 24, as compared to 124·1 for the week ended January 27.[141]

9·8 *Price Policy in 1960-61.* The upward trend of prices, specially because of the change in inter-sectoral relationship that appeared and seemed to have become entrenched, naturally caused concern as these were to a great extent a reflection of the pressure of continued expansion in bank credit and money supply. Steps were, therefore, taken to deal with the situation by further reinforcing official policies

140. Third Five Year Plan, p. 121.
141. R.B.I. Bulletin, March 1962.

on the monetary as well as non-monetary fronts. The measures of credit control adopted have already been analysed earlier (para 8). On the non-monetary front, the more important of the measures taken are listed below:—

(i) step up internal production of essential goods,

(ii) attempts to secure larger imports of foodgrains and industrial raw materials in short supply,

(iii) facilitate freer movement of foodgrains from surplus to deficit areas through a widening of the zonal arrangements,*

(iv) controlled distribution of available stocks of raw jute and raw cotton,

(v) steps to curb unhealthy speculative excesses in the various commodity markets.

9.9 *Trends in Cost of Living.* It is well recognised that cost of living index generally follows the trend of wholesale prices, except that exact quantitative relationship is generally absent due to differences in the items included and the weights attached. Food normally has the most preponderating weight and food prices have a great effect on the cost of living index number. For an appropriate study, we should have different index numbers to denote the changes in the cost of living of different income-groups of the population since consumption standards differ with income-range, so that as between two groups different items enter into final consumption and even for those commodities (or services) which are common, the proportion of the amount of their money income devoted for their consumption vary. It may be pointed out that although the Central Statistical Organisation of the Government of India conducted an all-India urban middle class family living survey as far back as 1958-59 in 45 selected centres, only certain preliminary results, based on incomplete tabulation† of the data collected, have so far been made available to the public. We have, therefore, not yet been able to get a series relating to consumer expenditure for the middle class and have only, as pointed out earlier, a consumer price index number for the working class. The trends of working class cost of living as indicated by this index number are indicated on the next page :—

* For Policy relating to foodgrains in 1960-61, See Vol. I, pp. 220-21.

† The Indian Statistical Institute, Calcutta are in charge of tabulation, Vide Monthly Abstract of Statistics, June 1960, p. (xi).

Consumer Price Index Number
(Working Class)

(Base : 1949=100)

Centres	1951	1956	1958	1959	1960	1961	Jan. 1962
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
All India Food	104	105	118	125	126	126	127
General	105	105	116	121	124	126	128
1. Ajmer	111	95	103	106	107	113	...
2. Bombay	108	115	129	134	137	140	135
3. Calcutta	104	98	110	110	113	114	114
4. Cuttack	123	106	116	118	127	131	124
5. Bangalore	115	114	131	140	146	150	...
6. Delhi	108	109	113	120	120	127	129
7. Gauhati	110	96	103	98	103	106	109
8. Hyderabad	108	116	123	129	132	137	...
9. Jamshedpur	116	106	123	125	120	123	126
10. Kanpur	94	89	98	98	99	102	107
11. Ludhiana	102	92	96	101	102	105	108
12. Madras	103	111	124	133	143	148	149
13. Nagpur	104	105	119	132	136	...	...
14. Jharia	116	87	108	108	105	...	...
15. Sholapur	105	106	105	114	119	...	...
16. Ahmedabad	105	98	110	125	120	121	...

Source : (1) State Governments.
(2) Labour Bureau, Ministry of Labour and Employment.

It will be seen that there is a very close correspondence between food prices and the general consumer price index. Further, there is a close directional correspondence between this index and the wholesale price index (*vide* para 9·7), though quantitatively there has been no exact correspondence, between the two, the wholesale price index being consistently lower than the consumer price index since 1956. There has been, however, a steady rise in the working class cost of-living index throughout the Second Plan period. In the earlier part of the Second Plan, the rise in the index of consumer prices was obviously because of the rising trend of foodgrain prices. This had created an impression in the country that food prices were at the bottom of all price rises.* This, however, has been proved to be a fallacy because the relative stability in food prices since 1959 has not prevented the cost of living from going up, indicating the pressure exerted by several other commodities which exert a basic influence on the cost of living.

* See Vol. I, Ch. V, para 3·3.

ed resources, a rise of prices, even when inflationary in nature, need not necessarily be the greater evil. Many of those who flinch in horror at the very idea of rising prices and who recoil at the faintest whisper of the word 'inflation' should realise that 'inflation' in the context of an under-developed economy is something quite different from the traditional concept of inflation in a highly developed economy, for, as has been pointed[144] out :

> "It is the full-employment inelasticity of output relatively to rising effective demand that serves as the criterion of 'true inflation' in the Keynesian sense, though Keynes allowed for the possibility of some inflation even before the full-employment level arising from specific bottlenecks. As far, however, as under-developed economies are concerned, the correct criterion of 'true inflation' is to be found in inelastic full-capacity output. For in these economies the lack of real capital, not of labour, is the ultimate bottleneck to 'real' expansion relatively to 'monetary' expansion."

It is indeed possible that some rise in prices may have to be solicited, along with its implications of rising profits to the private sector, as a means to securing expansion of physical volume of output and promoting domestic savings.

11. Planning and Controls.

11·1 *Coverage of Controls.* In the early stages of planning in India, there was a tendency to believe that planned development and controls were practically synonymous terms. The First Five Year Plan, for instance, argued that :

> "For one to ask for fuller employment and more rapid development and at the same time object to control is obviously to support two contradictory objectives."

Of course, the economic reasoning is really not so 'obvious', and the basic principle enunciated could be questioned, unless 'more rapid development' is interpreted to mean a rate of development more rapid than what would be realised without controls,—in which case, as the logician may point out, the fallacy of *petitio principii* is being committed. The point emphasised in the First Five Year Plan is, however, obvious, *viz.*, large scale planning does involve the inescapable necessity of controls, especially in a country where the

144. Kurihara—The Keynesian Theory of Economic Development, pp. 144-45.

private net product is still valued more highly than the social net product. Further, it is not correct to imply that planning alone necessitates controls, for, in India at least, the history of controls is older than the history of planning. Controls (in the widest sense of the term) were a product of wartime shortages initially, and, were later incorporated as parts of even non-plan normal administration under the Industries (Development and Regulation) Act, 1951, and, the Essential Commodities Act, 1955. The coverage of controls to-day is admittedly very wide, for

> "Government have powers to control prices and make allocations in respect of several commodities. Steel, cement, raw cotton, sugar and coal are in this category. Fertiliser prices are regulated through the Central Fertiliser Pool. Stabilisation of raw jute prices* through regulated purchases by the manufacturing interests is also envisaged. Both under the Essential Commodities Act, and under the Industrial Development and Regulation Act, the prices and distribution of a number of commodities are subject to control. Government can also adjust the rates of excise duty from time to time† on all excisable articles so as to alter suitably the relationship between particular prices."

It may be seen that the concept of controls in India is much wider than price-control, and there is a clear recognition that price-controls are unworkable without some sort of physical control.

11·2 *Unpopularity of controls.* One of the paradoxes of the administration of controls in India is the ceaseless attempt to reconcile two irreconcilables, *viz.*, efficacy and popular enthusiasm. Wedded as India is to the philosophy of a free democracy and the preservation of constitutionally defined fundamental rights, there is no escape from this dilemma. There is little illusion in responsible quarters that there are continuous efforts to circumvent the controls; yet, Government, as the custodian of the highest ideals of democracy, can hardly strive to increase the effectiveness of controls by reducing individual liberty and personal freedom, or by curtailing seriously the 'rule of law', even though it is recognised that "controls ineffectively or inefficiently administered may do harm rather than good". One can only hope

* Since introduced, vide Report on Currency and Finance 1960-61 p. 28.

† Along with Budget proposals.

that with better understanding of the purpose of controls and a fuller realisation of their nationally beneficial aims, public resentment against controls would be gradually overcome. It seems necessary therefore, to adopt a three-pronged attack against the present popular prejudice against controls, *viz.*,

(a) wide publicity of the purpose and benefits of control measures,

(b) stringent measures against corrupt practices in the administration of controls, and

(c) drafting control measures sufficiently carefully so as to leave fewer loopholes for legal evasion.

Further, to be successful, control measures must be economically rational, for in the realm of economic activity power comes through wisdom and not from authority, and no amount of either wishful thinking or the pompous dignity of frowning authority would make the system work for long against the laws of economics. It is a pity that the sane dictum outlined in the First Five Year Plan, has not always been borne in mind, *viz.*,

> "......it is an essential condition that the rationale of each control is made clear to the public and the rights and obligations of the parties affected defined in a manner which leaves little scope for doubt as to what is expected of the public and where redress may be had in case of any grievance. It is also vital to the success of controls to make necessary adjustments in their working from time to time as the conditions governing the supply and demand of the commodities in question change".

11·3 *Statutory basis for Controls in India.* We have discussed earlier the nature and extent of import control, exchange control and credit control, each one of which derives its authority and basis by virtue of powers specifically assigned to the appropriate body. In the field of internal trade, controls emanate from the following main sources :—

(1) price fixation by the Tariff Commission in accordance with the statutory provisions of the Tariff Commission Act, 1951 ;

(2) powers under the Industries (Development and Regulation) Act, 1953, which empowers Government to regulate supply and distribution, and, Trade and Commerce, in any commodity for which it is necessary to do so in order to secure equitable distribution and availability at fair prices,—the

article or class of articles must, however, be related to a scheduled industry as defined in the Act ;

(3) authority derived under the Essential Commodities Act, 1955, which enables Government to provide for regulating or prohibiting the production, supply and distribution of, or, Trade and Commerce in, any essential commodity* for which Government felt the necessity of maintaining or increasing supplies or desired to ensure equitable distribution and availability at fair prices ;

(4) regulation of "Forward" markets under the Forward Contracts (Regulation) Act, 1952, to be administered by the Forward Markets Commission.

11·4 *Economic basis of Control Operations.* Direct physical controls seek to allocate limited supplies to an extracted lower volume of demand where supply is inadequate to meet the entire demand through the mechanism of the market. price controls, on the other hand, seek to bring about an altered balance between supply and demand by disturbing the relationship between the production of the controlled commodity and other commodities. In either case, the basic economic principle is to prevent all those units of demand which have a higher marginal demand price, but lower social value, from commanding the limited and scarce supply. It is clear that except where the controlled price is higher than the free market price, price control must mean that demand at the controlled price is in excess of supply at that price. If so, unless price control is accompanied by controlled distribution and rationing, "black" market prices must emerge to equalise supply and demand ; or, supply would be artificially augmented at the controlled price by lowering the quality of the product, *i.e.*, by substituting a cheaper supply. It is apparently futile to control prices without controlling distribution (and also, perhaps, production) for one cannot disturb price and expect that the forces of supply and demand, even when unchanged, would find an equilibrium also at the disturbed price. Controls are, therefore, like skating down a slippery path—there is no stopping till one has gone down fully.

11·5 *Chief criticisms against the Administration of Controls.* Direct physical controls are always open to administrative abuse, especially if supplies available are excessively short, for no equitable principle of distribution can be developed if the quantity available is below the minimum

* The Act gave a long list of essential commodities which covered practically all items except luxury goods, and, gave also the power to notify any other commodity as essential.

necessary.* The abuses also emerge because of the large number of persons involved and the complicated hierarchy through which controlled distribution must take place. Further, the private sector has also to be utilised in the channel of distribution and it is difficult to ensure high standards of honesty in all cases ; though, it must be admitted that harrasment of the small trader by the petty official is not unknown. Thus, direct physical controls are difficult to administer in a big country like India, not only because of its size and large population but also because of the comparative lack of education amongst the people and the unavoidable use of a large army of low-paid petty officials.

So far as price-controls are concerned, the real difficulty lies in fixing the appropriate price. If the economy is left to work itself through consumer's preference and producer's desire to derive maximum revenue, the price of each commodity gets itself adjusted in the long run to every other price in such a way as to secure equilibrium of demand and supply for each commodity. In other words, in an integrated economic system, prices are inter-related and no one price can be treated in isolation, as each price is part of a structure of prices. A controlled price must obviously disturb this inter-relation. The disturbance would be greater in a period of general uptrend of prices brought about specially by inflationary tendencies rather than by changes in physical availabilities, than in a period of comparative stability of the price-level. From the point of view of economic theory (and what is true of theory must necessarily be true in practice also) it is necessary to ensure the least disturbance in the relationship between controlled prices and noncontrolled prices; otherwise, to make controlled prices effective, physical controls would be inescapable. At this stage the sceptic may wonder as to the necessity of price-control at all if controlled prices should be as near to the natural economic price. The answer lies in the interpretation to the concept of natural economic prices. If by that phrase is meant prices that would be brought about by allowing conjunctural short period calamities to be exploited by unscrupulous sellers, then the theory of controls goes overboard. But no social economist of today would accept such an extreme position, and, to most, controlled prices are a device to secure a workable compromise between private gain and social good. It, therefore, follows that controlled prices must be some sort of "fair

* When I was Deputy Commissioner, Sambalpur (Orissa), in 1952, a Civil Supplies inspector asked me during one of my tours in the interior to enlighten him on the best principle of distributing 5 sarees amongst 62 adult women. I frankly pleaded inability.

prices"—fair to the producers, fair to the consumers, fair to the requirements of development and fair to the changing circumstances and needs of the economy. It is admittedly difficult to give practical quantitative expression to the notion of "fair" prices. The Tariff Commission is the statutory agency for fixation of fair prices and since its inception in 1951 it has undertaken a large number of enquires relating to price-fixation. The composition of a fair price is a debatable question, and it is not surprising that the procedure adopted by the Tariff Commission in its various enquiries has not only been not uniform but has also come in for considerable criticism.[145] Search for agreement on this question is apparently futile and Government can only choose the best people to serve on the Tariff Commission and, thereafter, leave it to the judgment and integrity of the Statutory machinery set up by due process of law. It is not implied that the Tariff Commission has been, in all cases, infallible; all that is being argued is that the Government has no other alternative, though it must undoubtedly play its own part properly by putting on the Tariff Commission only people of unquestioned ability and high integrity and who are capable of withstanding pressure from all quarters.

11·6 *Open Market Operations in Controlled Commodities, Particularly Foodgrains.* The problems of state trading have been considered earlier. It has been pointed out that through the operations of the State Trading Corporation, it may be possible to stabilise prices, of particular commodities at least, in the internal market. In the context of price control, open market operations in foodgrains has an important part to play. Also, apart from controlling food prices, there is the more important problem of securing appropriate inter-regional distribution of food supply and ensuring movement from surplus areas to deficit areas. Again, there is the question of getting food supplies from abroad to secure a balance between all-India needs and our total production*. Finally, there is the necessity of building up buffer stocks. It has been generally recognised that Governmeut can hardly leave food prices and food supply to be determined entirely by private trading. The growth of urbanisation in India, coupled with an increase in self-consumption in the rural producing areas, makes it in-

145. See article in Tata Quarterly, January 1962; the author, naturally, holds the view that the approach in the 1955 Rubber Tyres and Tubes Prices enquiry was scientific.

* Statistically, according to the N.S.S. Data, we do not need food imports, which however, have been substantial during the Second plan period! See Vol. I, p, 216 for per capita availability of food.

cumbent on Government to ensure proper availability of food at reasonable prices. The Third Five Year Plan stated the policy approach regarding food in the following words:

> "In an economy like ours where a substantial proportion of the expenditure incurred by families in the low income ranges is on food-grains, reasonable stability of foodgrain prices is of vital importance. The experience in this field over the last decade and more has shown clearly that this is a field in which neither complete control nor complete decontrol are feasible. Government must always be in a position to regulate effectively the course of foodgrains prices".

Any effective open market operations in food grains requires substantial buffer stocks and operating on them through continuous purchase and sales over a wide front. Further, the operations are not identical all over the country at any given time. Differences of geographical and climatic conditions, varying stages of economic development and unequal densities of population, make India "a world unto itself" where movements of prices are not exactly uniform. As food prices vary between different places, it might be necessary to buy in some parts and sell in some others simultaneously. This requires a widespread network of storage facilities and an administrative organisation highly sensitive to market changes. The task is not easy, but it has to be undertaken if Government is to prevent antisocial activities like hoarding and profiteering from getting the upper hand.*

11·7 *Conclusion*. Controls appear to be unavoidable. As they are also fraught with danger, they must be operated with caution. Infallibility cannot be claimed for any organisation, not even for a Government dedicated to the welfare of its people, but competence and integrity are legitimate expectations, not beyond realisation. The tasks are difficult and should be approached in a spirit of humieity, with emphasis on control on "controls", for, otherwise, controls like Frankenstein, may destroy its creator.

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* The problem of Food supply has been enalysed fully in Vol. I. See Ch. V, particularly paras 4·4 and 4·5.

X

THE BANKING SYSTEM

1. Nature and Functions of Banking.

1·1 *The Concept of Banking.* As an integral part of the economic system, banking owes its significance to the growth of the habit of settling claims against one another by the transference of, not legal tender currency but instead, claims to money. The use of claims on money to settle transactions is synonymous with the emergence of money as a link between value surrendered and value acquired through an economic transaction in which the unit of money used is not wanted for its own sake but for the purchasing power it commands. Thus, with the decline in the significance of the intrinsic value of money for purposes of enabling money to discharge its functions, it became immaterial as to whether one used legal tender currency, which itself to-day is token money or fiat money with the intrinsic value of the material substance of which it is made divorced from its monetary face value, or a claim to it, which conversely is a title to a debt allegedly binding on a bank. It is the growth of this characteristic in the economic system which laid the foundations of modern banking, though original banks did, probably, came into existence as dealers in precious metals, remitters of "value" from place to place and providers of safe custody for valuables along with usurious lending.

1·2 *Meaning of Bank-Money.* Bank Money is non-legal tender money held in the form of deposits, which it is convenient to designate as member-bank-deposits following the American custom and in view of the fact that these banks constitute an important part of the structure through which the Central Bank controls the monetary system. The deposits of a banking system are not entirely the result of passive acceptance of cash savings or transference, for holding, a legal tender money from the public to the bank. They are also actively created by the banks themselves through the granting of loans and advances. Once, however, a given volume of bank-money has come into existence, the whole of it can be used for settlement of transactions and it is immaterial as to what

part of it represents passive deposits and what part has been actively created. The modern banking system can thus play an important part in enlarging or contracting the volume of available bank-money for enabling the economic system to function, though in the ultimate analysis there does exist a broad link between the volume of legal tender money in a country and the total volume of money supply including bank money. Since the person accepting bank money is not aware as to whether it is a part of passive deposit or a part of actively created deposits (nor, in fact, does it matter to him which part it represents), all that he expects is that, when presented, it would be convertible into legal tender money, if required. Thus a person accepting bank money is accepting a debt of the banker to somebody else, and it is obviously immaterial whether the debt originated by the bank accepting a deposit and incurring a debt, or, by the bank granting a loan and creating a debtor to it. The circulation of bank money, therefore, is synonymous with faith in the debt being encashed, when required, in money. Thus, "the use of Bank-Money depends on nothing except the discovery that, in many cases, the transference of the debts themselves is just as serviceable for the settlement of transactions as is the transference of the money in terms of which they are expressed. A title to a debt is a title to money at one remove, and, to the extent and within the field that confidence is felt in the prompt convertibility of the debt into the money, the element of remoteness is irrelevant to the serviceability of Bank Money for settling transactions."[146]

1·3 *Functions of Banking*. Banks perform a variety of functions in the modern economy and, to a great extent, not only is the development of the economy assisted and promoted by banking, but one might say also that the extent of the use of banks and bank money is itself an index of the state of development of an economy. The functions of a bank may be broadly indicated as follow :

I. *Pure banking functions—*

(i) receipt of deposits both on current account and fixed deposit account,

(ii) discounting of bills and promissory notes,

(iii) granting of loans,

(iv) issuing of drafts, letters of credits etc., and, arranging to remit money from place to place,

(v) acceptance, on behalf of customers, bills of exchange ;

146. Keynes—Treatise on Money, Vol. I, p. 15.

II. *Agency service functions—*

(vi) collecting and paying of cheques,

(vii) acting as trustee or executor of its customers,

(viii) collecting of dividends, interests etc. on stocks and securities held on behalf of customers,

(ix) making periodic payments, as per standing instructions of customers, of subscriptions, insurance premiums etc ;

III. *General utility service functions—*

(x) issue of credit instruments,

(xi) transaction of foreign exchange business,

(xii) rendering safe deposit facilities for valuables etc.

The above classification of functions* is purely for convenience of enumeration, for clearly some of the functions overlap with one another. However, detailed enumeration of the functions of a bank is useful, for sometimes a bank is defined (rather described) by the functions it performs ; for example, the definition used in an U.S. Act of Congress runs as follows :

> "By 'banking' we mean the business of dealing in credits and by a 'bank' we include every person, firm or company having a place of business where credits are opened by the deposit or collection of money or currency, subject to be paid or remitted upon draft, cheque or order, or, where money is advanced or loaned on stocks, bonds, bullion, bills of exchange, or promissory notes, or where stocks, bonds, bullion, bills of exchange, promissory notes are received for discount or sale."

This is as good a list of functions of a bank as any that one can visualise, and brings out the fundamental points *viz.*:

(a) that banks are institutions which carry on operations of giving as well as receiving credit, and

(b) that banks are institutions that function with borrowed funds rather than owned funds as distinguished from moneylenders, though accumulated profits over time do increase steadily the significance of owned funds for a bank.

2. The Indian Banking System.

2·1 *Structure and Organisation.* The banking system in India has been influenced considerably by historical growth

* The reader may at this stage acquint himself with the elements of banking ; See Walter Leaf—Banking.

and past traditions, and is to-day a peculiar adaptation of the U.K. model with specific Indian characteristics interwoven. Following U.K. practice, India has developed a system of commercial banking based mainly on the oraganisation of joint stock banks. In addition, we have what are historically known as the Exchange banks as also a giant state owned commercial bank in the State Bank of India. There are the specialized co-operative banks and the institutions for industrial finance working more or less on a formal organised basis and modelled to a great extent on western lines. In addition, we have the unique institution of Indigenous Banking, though even to-day controversy rages round the age-old question of whether to regard him as a banker or a moneylender. Thus the constitutents of the Indian banking system are :

1. The Commercial Banks, consisting of :
   (a) Indian Joint Stock Banks
      (i) scheduled banks
      (ii) non-scheduled Banks,
   (b) Exchange Banks, *i.e.* Indian branches of foreign banks ;
2. The Indigenous Bankers ;
3. The specialized agencies of finance, comprising of :
   *A. Rural Finance.**
      (a) Co-operative Banks,
      (b) Land Mortgage Banks,
   B. Industrial Finance†
      (a) Industrial Finance Corporations,
      (b) State Finance Corporations ;
4. The Post Office Savings Banks ;
5. The State Bank of India ;
6. The Reserve Bank of India.

Of the above, the State Bank of India performs functions similar to those of commercial banks, but because of its special position and structure, it is better to study its activities separately. The Reserve Bank of India is, of course, the head of the system and performs the functions of a currency authority and discharges central banking obligations. The Government Post Offices are performing banking functions in the sense of accepting deposits and mobilising savings, but

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* See, Chapters III and IV.
† See, Chapter VI.

they do not undertake the lending functions or the various other subsidiary functions of banks. So far as the Indigenous bankers are concerned they certainly perform practically all the functions of organised banking, including in some cases acceptance of deposits, but they are usually regarded as a part of the unorganised sector of Indian banking and do not come under the same type of formal control of the Reserve Bank of India as the organised banks do.

2·2 Trends in Indian Banking Development.

2·2·1 *Growth of Bank Money.** The proportion of economic transactions covered by bank-money in India is comparatively low, and, transactions in money still play a significant part in the Indian economy. In this respect, India is comparatively backward, for in western countries and the more developed economies of Australia and Japan, bank money preponderates and the use of currency is insignificant. The comparatively minor role played by bank money in India is illustrated in the table given below :—

(Crores of Rupees)

Last Friday of Year	Total Money Supply with the Public	Currency with the Public	Variations in (3)	Deposit Money with the Public	Variations in (5)
(1)	(2)	(3)	(4)	(5)	(6)
1950-51	1,971·06	1,330·76	+ 81·72	640·30	+30·93
1955-56	2,184·45	1,505·22	+193·89	679·23	+70·37
1956-57	2,312·88	1,556·49	+ 51·72	756·39	+77·16
1957-58	2,389·35	1,607·13	+ 51·29	782·22	+25·83
1958-59	2,499·59	1,725·36	+117·90	774·23	− 7·99
1959-60	2,703·13	1,862·72	+138·79	840·41	+66·18
1960-61	2,901·72	2,026·89	+167·05	874·83	+34·42

Source : R.B.I.

It is apparent that not only is bank money in India far less important than currency, even its growth during the last decade has been unable to keep pace with the growth of currency. It should, however, be recognised that the poverty of the Indian masses, their lack of literacy and the low unit value of a large proportion of transactions in the country restricts the use of bank money. Further, some major bank

* For Statewise detailed statistics, See Vol. I, Ch. I, Tables 13, 13 A and 14.

failures in living memory have shaken the confidence of the public, and it is, therefore, not surprising that inspite of modernisation of the economy, the switchover from currency to bank money has been comparatively slow.

2·2·2 *Growth in Numbers.* Judged by the growth in the number of banks, the position is still more unsatisfactory and one may be tempted to argue that since the basic structure of banking is not being properly developed, it is doubtful whether the switchover to the use of bank money would take place in the foreseeable future.

Number of Banks

Type of Bank	1951	1955	1958	1959	1960
(1)	(2)	(3)	(4)	(5)	(6)
1. Indian Commercial Banks					
(a) Scheduled banks	76	72	77	78	77
(b) non-scheduled banks	469	365	278	265	252
2. Foreign Banks					
(a) Scheduled banks	16	17	16	16	16
(b) non-scheduled banks	5	1	—	—	—
Total	566	455	371	359	345

(Source : R.B.I.)

The information revealed by the above table indicates some paradoxical developments. The number of scheduled banks have remained practically stationary at the end of the decade as compared to the beginning, but during the same period the number of non-scheduled banks has gone down significantly. This may partly be due to amalgamations and increases in size, which is a trend for the better, and, partly due to a policy of discouragement to the very concept of non-scheduled banks in the country.

2·2·3 *Development of Branch Banking.* It might be emphasised that the total number of banks in the country is not a complete indicator of development, for one must take note of the development of branch banking, especially as spreading a net work of branches in the interior is essential for spreading banking habits in the country.

Number of Banking Offices

Types of banks	1951	1955	1958	1959	1960
(1)	(2)	(3)	(4)	(5)	(6)
1. Indian Commercial Banks					
(a) Scheduled banks	2581	2791	3563	3860	4080

(1)	(2)	(3)	(4)	(5)	(6)
(b) non-scheduled banks	1463	1141	862	828	789
2. Foreign Banks					
(a) Scheduled banks	65	67	66	66	69
(b) non-scheduled banks	6	1	—	—	—
Total	4115	4000	4491	4754	4938

(Source : R.B.I.)

It is clear that the total number of bank offices has increased fairly satisfactorily; but the more satisfactory trend was the increase in the number of offices of Indian scheduled banks. Since the total number of Indian scheduled banks remained practically constant during the last ten years, the increase in the number of bank offices is an unmistakable sign of the development of branch banking[147] in the country. This is a healthy development for generally the vulonerability of the banking system is reduced with the growth of branch banking, which also leads to greater mobilisation of savings and better flow of funds between surplus savings areas and deficit investment areas. Branch banking is possibly less costly to maintain and, therefore, tends to reduce the ratio of costs to total business to less than what it would be if independent banks were to multiply and command the same aggregate volume of total business. It might be argued, as has indeed been maintained by supporters of small scale operations, that independent banks are usually more active in promoting new business and would, therefore, develop aggregate business faster. Such a contention is contrary to the lessons of history, for in India at least, small banks have been models of inefficiency, nepotism and patronage, and unbusiness like investment causing considerable loss of national resources, to say nothing of the great hardship caused to many small depositors whose life's savings have been practically wiped out due to bad management.*

2·2·4 *Growth of Deposits.* The function of deposit creation, whether passively or actively, constitutes a primary function of banking system. It must be borne in mind that the popular conception of a large deposit as indicative of effective promotion of savings or as an index of the strength of a bank is fallacious. To the extent deposits are created through loans and advances, it is an investment for the bank, and, whether such deposits constitute a source of strength or of weakness depends on how wise or how foolish the bank's lending policy has been, for the larger the percentage of likely bad debts the greater is a created deposit a potential source of

147. For advantages of branch banking, see Sayers-Modern Banking pp. 23-24.

* For State-wise distribution of bank offices, see Vol. I, p. 65.

weakness and danger for the bank. Again, it is popularly believed that time-deposits represent savings, while demand deposits indicate loans given. There is no foundation for such a belief. It may be true to a limited extent that a larger proportion of time-deposits is the result of refraining from current consumption and is held as a sort of savings for the rainy day, but it would certainly be inaccurate to correlate savings with any particular movements of time-deposits and demand-deposits relative to each other. Similarly, while a larger proportion of demand-deposits may possibly be the result of loans and advances, it would be a mistake to associate every increase of demand-deposits as a sign of increase in loans granted, for it could equally well be a sign of increasing liquidity preference of the public, and represent savings which might otherwise have gone to swell time-deposits. It may, therefore, be emphasised that the distinction between these two types of deposits, while important for purposes of judging the nature of the liabilities that the bank is carrying and significant for assessing the adequacy or otherwise of the reserve ratio's of banks against their liabilities, is unimportant for assessing the extent of mobilisation of resources that the banking system has undertaken. The aggregate figure of deposits, however, does provide an index to the part played by the banking system. So far as the economy as a whole is concerned, and, a rising volume of aggregate deposits, assuming that the loan policy of the banks is not more unsatisfactory than it was before (or, more positively, has remained as satisfactory as previously), does indicate a more extensive service rendered to the community. Since a major problem for planning in India is increasing the rate of domestic savings, it is a matter for serious consideration whether the banks should not be compelled to publish separately figures of their passive deposits and created deposits, rather than to leave it to be derived (rather unsatisfactorily) from figures of loans etc. published otherwise.* However, a statement is given on the next page of the deposits of the banking system for what they areworth.

The steady upward trend, which was fairly rapid during the Second Plan period, seems to have been upset in the last year of the Second Plan, as 1960-61 figures show a decline, though only marginally. As full figures for 1961-62 are not yet available, it is difficult to say whether the setback will be recovered and a positive gain forward made in 1961-62 over 1959 60, but, if deposits of the banking system in 1962-63

* An interesting exercise would be to try and reconstruct the figures of deposits as a result of cash tendered from Statements 28 and 29 published in the Report on Currency and Finance, (1960-61).

at the latest do not recover and rise above the peak level reached in 1959-60, it would be a serious concern.

Deposits

(Rs. Lakhs)

Year (Last Friday of March)	Indian Scheduled Banks	Non-scheduled Banks	Total
(1)	(2)	(3)	(4)
1951-52	632,93	58,81	691,74
1955-56	814,96	66,81	881,77
1957-58	1187,72	46,41	1234,13
1959-60	1614,43	50,09	1664,92
1960-61	1586,66	42,73	1629,39

Source : R.B.I.

2·2·5 *Growth of Savings Deposits.* From a strictly analytical point of view, figures of Savings Deposits do not provide any accurate index to total savings promoted by banks, except, as pointed out earlier, there could be a presumption made (not unjustifiably) that larger savings would normally go to increase the savings deposits with the banks. One could, therefore, perhaps argue that growing figures of savings deposits, especially during a period of overall rising prices with a mounting tendency towards greater liquidity preference on the part of the public, are a sign, though imperfect, of a rise in domestic savings. However, the assumptions and qualifications are so many that the figures given below should be interpreted with great caution.

Savings Deposits with Scheduled Banks

(Lakhs of Rupees)

Year (Last Friday)	Indian Scheduled Banks	Foreign Banks	Total
(1)	(2)	(3)	(4)
1955-56	155,01	14,42	169,43
1956-57	175,01	15,62	190,61
1957-58	190,80	17,34	208,14
1958-59	208,94	19,84	228,78
1959-60	231,67	21,69	253,36
1960-61	256,16	25,65	281,81

Source : R.B.I.

3. Safety in Banking.

3·1 *The Concept of Safety.* Good banking is not necessarily synonymous with safe banking, if safety is defined as merely ability to repay all deposits when due. If safety in banking were to be interpreted in that narrow and restricted sense, a perfectly safe bank would hardly make any contribution to the development of the economy and would earn for itself little profit. It is, of course, not implied that one could conceive of a bank as being good and yet unable to meet the day to day demands for withdrawal made on it ; what is being suggested is that all deposits due for payment on any particular day is not necessarily equal to all likely withdrawals on that day, and, economic safety in banking consists of providing for the latter and not for the former. In other words, good banking involves the estimation, as accurately as possible, of the maximum potential withdrawability of funds at every point of time and making provision for meeting such demands at each point of time. Thus, safety in banking may be regarded as constituting :

(a) a recognition that a bank must be safe (in the sense defined above) at every point of time and not merely in the long run ; that each and every bank must be so safe, for safety of the banking system as a whole is a misnomer ;

(b) a careful estimation of likely normal demands for net withdrawal from a bank each day ; and

(c) a provision of adequate cash in legal tender money to meet promptly all such withdrawal.

It is obvious that the crux of the problem lies in (b) above, and since laws cannot provide for such wisdom, we have the famous dictum of Hartley-Withers to the effect that sound banking depends not on good laws but on good bankers.

3·2 *Economics of Safety.* Every excess cash reserve over and above normal daily requirement is idle cash and involves locking up of funds instead of using them for profitable investment ; at the same time, every investment which restricts availability of cash when required endangers safety. Thus, the dilemma of modern banking is the reconciliation of profitability with safety, and, to arrive at the optimum distribution of resources between different types of investments and maintenance of cash reserves. The problem of the investments would be taken up for consideration separately, but at this stage it may be noted that neither the profitability of the total volume of investment nor the profitableness of investment in any particular direction is a

constant factor. It changes with every change in the economic situation, so that the alert banker has always to be on the look out for opportunities for expansion (or, if necessary, the need for contraction) in his total investments, and to shift his investments from one direction to another. Thus, sometimes it may so happen that a banker may perforce have to keep a larger cash reserve than he need keep, though such a contingency is unlikely in an expansionist economy. As regards his proper cash reserve, it may be pointed out that in calculating its appropriateness a banker must necessarily assume continuance of normal conditions for no anticipatory action against sudden and unforseen abnormalities can be a part of normal banking operations.

3·3 *Factors affectng Cash Reserve*. A bank is every day constantly paying out cash and receiving it. Further, as some cheques drawn on it may be deposited in other banks, similarly cheques drawn on other banks may be deposited with it. This is the inevitable result of distribution of clientele as between a number of banks in the banking system. A bank, therefore, would be constantly required to meet claims from other banks simultaneously with receiving claims against other banks. Obviously, the art of banking would be to equalise, as far as possible, these opposing trends so as to minimise excess cash kept idle. It is necessary to understand the considerations which underlie decisions as to the amount of cash reserve to be kept. The principal circumstances which influence the reserve requirements may be summed up as follows :—

(1) habits of customers. Normally, withdrawability of funds is greater if customers are not used to circulating cheques ;

(2) business conditions of the locality. Generally, a manufacturing and commercial community has more numerous and frequent transactions, which might necessitate a relatively larger cash reserve ;

(3) seasonal demands. In agricultural communities demand for cash is high when crop movements are being financed than during the slack season when crops are growing ;

(4) religious and social festivities, and, requirements of holiday seasons. It has been found that more cash is generally needed just before *Diwali* and when the summer exodus to the hills takes place ;

(5) availability of clearing house facilities. This reduces the requirement of cash, for with this facility only the net difference between cheques drawn against

and in favour of a bank has to be provided. In the absence of clearing house facilities, the entire volume of cheques drawn against has to be provided in cash, for no bank could be certain of collecting the cash on cheques drawn on other banks held by it before it is required to honour the cheques drawn upon it;

(6) nature of accounts. It is well known that salaried account holders draw less frequently in cash than business account holders, particularly those engaged in speculative transactions ;

(7) size of deposits. It has been found that the need for cash reserve is greater in the case of larger deposits than for small deposits ;

(8) number of accounts. The larger the number of accounts, the less is the requirement of cash because there is a smaller likelihood of any general movements for encashment of deposits ;

(9) conventional amounts kept by other banks and the need for "window-dressing". It is generally impossible for any particular bank to keep a cash reserve at a very much lower figure than that maintained by other banks because of the necessity of maintaining the confidence of a somewhat irrational public;

(10) legal requirements. Where the law requires a prescribed cash reserve ratio, the minimum so prescribed no longer remains within the discretionary calculation of the banker.

The various considerations outlined above would seem to indicate that if cash reserves were to be rationally determined, they should vary from bank to bank, and, vary from time to time even for the same bank. However, strangely enough, the actual fact is quite otherwise, *viz.*, the cash reserve ratios have a strange constancy over time and a peculiar uniformity from bank to bank. There is a tendency to fix a ratio (hit upon one would, perhaps, be a more realistic way of expressing it) and then to permit only moderate departures from time to time.

3·4 *Cash Reserves—the Facts.*

3·4·1 Banking practices do not exist in vacuum, they are influenced by the economy in which they function. In the past banking practices changed slowly and imperceptibly because the economy itself changed gradually. Such, however, is not the case any longer. State interven-

tion and planning are rapidly altering the face of the country, and, in one decade India has changed radically, perhaps more significantly than she did during the first half of the twentieth century. In the field of banking also, rapid and revolutionary changes have taken place with the Reserve Bank of India entering into its true role of developmental banking and the Government providing a new framework of banking law for the system to work under. The economic integration of the country has made the different economic regions to come closer, and with the development of branch banking, quicker remittance facilities and availability of reliable credit facilities from the Reserve Bank of India (both normally and in emergencies) the regional differences in banking practices that existed prior to 1950 are on the decline. The cash-ratios of individual banks, therefore, have ceased to be significant for studies relating to banking practices, and it is doubtful whether they are of much importance even from the point of view of the safety of particular banks as investment policy rather than the cash-reserve ratio has proved to be the deciding factor for the efficiency of a bank. The cash-reserve ratio of the aggregate banking system would, therefore, appear to be now a more fruitful object of study than cash-ratios of individual banks.

3·4·2 In the analysis of the problem, it would be enough to confine detailed attention to only the scheduled

Ratio of Cash to Aggregate Liabilities
(cash means cash in hand and balances with Reserve Bank)

(Rs. Lakhs)

Year (Average of Fridays)	All Scheduled Banks	Indian Scheduled Banks	Eoreign Banks	Aggregate Liabilities of (3)	Aggregate Liabilities of (4)
(1)	(2)	(3)	(4)	(5)	(6)
1951-52	11·03	11·48	9·22	687,90	171,30
1955-56	8·69	9·05	7·16	811,65	191,89
1056-57	7·96	8·11	7·26	906,56	188,35
1957-58	8·89	9·04	8·09	1,108,07	208,61
1958-59	8·03	8·11	7·46	1,342,24	206,63
1659-60	6·75	6·80	6·38	1,570,03	216,75
1960-61	7·33	7·30	7·56	1 679,06	235,95
1961-62	6·46	6·54	5·93	1,694,88	256,71

Source : R.B.I.

N.B 1. Figures relate to business in India.
2. The figures for average of Fridays are a better guide for this purpose than the figures of last Friday of the Year.

banks, since the business of the non-scheduled banks is a tiny fraction of the total deposits in the country. Again, it seems better to consider the ratio of cash to aggregate liabilities rather than merely aggregate deposits, though the latter without doubt constitute the lion's share of the former. The table on previous page illustrates the position :

Two conclusions emerge from the above table, *viz* that

(a) there is a tendency towards a steady decline in the cash-reserve ratio,

(b) Indian banks keep a higher cash-reserve ratio than foreign banks.

There is nothing unsatisfactory in either of these trends, both of which are consistent with the changing course of economy and banking in the country. It is clear that with the growth of banking habit, the use of cheques must rise and with it there should normally be a decline in the encashability of cheques drawn, *i.e.* more and more cheques would tend to be redeposited so that there would be only transfers of deposits as between banks and individuals rather than conversion of cheques into cash. This, together with the available assurance of credit facilities from the Reserve Bank of India must logically lead to a decline in the ratio of cash maintained. It is also not unusual that foreign banks should keep a lower cash-reserve ratio, for public confidence[148] in them is still higher than in private Indian banks partly because of past history of Indian bank failures and partly justifiably so because of a sounder investment policy pursued by them. However, the gap between the two ratios is steadily on the decline and in the foreseeable future, perhaps, it would be unnecessary to have figures in three columns for such a study.

4. Bank's and Economic Uses of Funds.

4·1 *Banker's Responsibility.* In the matter of uses of funds, the banker has both a national responsibility and a particular responsibility. The funds made available to the banking system no doubt primarily belong to individuals, but they are also a part of the resources of the nation. It is not unreasonable to expect, in the context of planned development with a low availability of domestic resources, that the banking system should make the best national use of the resources available to it, consistent, of course, with the minimum interests of the individual depositors and the bank

148. For an excellent analysis of factors determining confidence, See, Muranjan—Modern Banking in India pp. 322-338,

itself. In other words, neither safety nor profitability constitute the be-all and end-all of a bank's investment policy, for the country is entitled to demand that resources of the banking system shall be used to further the development of. the country along the objectives laid down in its planning policy. In 1931, the Foreign banking experts[149] invited to assist the Indian Central Banking Enquiry Committee stated in their report :

> "We endeavoured to take into account the specific circumstances prevailing in India and to adjust our views accordingly, but we cannot accept recommendations, which are, in our opinion unsound and contrary to banking principles which ought to be adhered to under all circumstances and in all countries. Our conclusions are based on these principles and we cannot concern ourselves with ambitions or desires of a political or nationalistic character."

With the first part of the view expressed above, there would be general agreement. No sane social economist would ever dream of using the banking system contrary to sound principles of commercial banking, especially as such a use would be against the long period national interest itself. With the second part of the views of the foreign banking experts,* there can be a legitimate difference of opinion, and one could maintain, (in fact, in the context of Indian planned development, one should maintain) that where alternative uses of funds are available banks must give preference to those that are consistent with the objectives of the plan and further its targets. The choice is obvious where the alternatives are equally profitable ; it is equally apparent where there is no lack of safety, though lacking in a high rate of profitability, with the required minimum economic return. It is not unreasonable to impose a sacrifice on the banking system (and, via it, on those who would otherwise have profited a little more as individuals) in the national interest. The banking system must increasingly acquire a public purpose in their activities, for only by acquiring such a purpose can it legitimately claim to be allowed to continue outside the public sector.

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149. Report of the Indian Central Banking Enquiry Committee, p. 607.

* Strangely, at the same time the Macmillan Committee on Finance and Industry in England were holding that an additional burden on the banks could be "justified in the public interest." See Report, p. 158.

4·2 *Investment Distribution of Assets.* The funds of a bank can be utilised profitably in the following directions :

A. Creation of bank credit

(1) Loans and advances, including cash credits and overdrafts, *i, e.* creation of active bank deposits ;

(2) Purchase and discount of bills ;

B. Purchase of Securities

(3) Investments in Government securities ;

(4) Transactions in stocks and shares, *i. e.* investments in variable yield securities ;

C. Short term lending

(5) Balances with other banks, mostly in current account ;

(6) Money at call and short notice.

Like most fields of banking, the structure of assets of a bank involving the profitable uses of funds is not capable of being laid down in a cut and dried formula. It involves the exercise of considerable judgment in which the conflicting claims of safety and profitability have to be balanced, and true national interests recognised. In the field of investment distribution, the banker must act as an agency for social welfare, furthering the aims of planned development, within the framework of private sector banking which cannot completely eschew considerations of profit. The Indian banking system has a peculiar composition in this respect. One of its constituent instutions, in fact the biggest brother *viz.*, the State Bank of India, is in the public sector while the remaining ones are in the private sector. This mixed composition is both an advantage and a disadvantage. On the one hand, it is easier for the banking system to easily recognise the lead of the State Bank of India in the matter of public policy ; on the other hand, there is the obvious temptation of leaving to it the burden of public policy while the cream of economic returns may be bagged by private sector banking.

4·3 *Principles of Distribution of Investments.* There is, it may be emphasised at the very outset, no such thing as a theoretically ideal principle of distribution. No distribution is ideal by itself, for it is influenced considerably by circumstances in each country, changing conditions of the economy and even by the particular problems of each bank. The position was ideally put by Prof. Muranjan[150] as follows :

150. Modern Banking in India, p. 130.

> "The financial and economic structure of each country prescribes in a broad manner the character of resources which banks attract and the type of investments in which their funds find outlet. Within the limits set by the financial and economic structure, each bank and banking system have to strive to reach a balance, often a very delicate one, between a maximum of profit and a maximum of liquidity and elasticity. The factors which underlie the financial and economic structure are themselves liable to large cyclical and secular changes amidst which eternal vigilance and adaptability are the only key to success in banking."

It might be added that "the emergence of planning slightly alters the emphasis since the objective of planning must be to reduce significantly, if not eliminate altogether, "large cyclical and secular changes"; but, planning at the same time imposes new obligations in the shape of recognition to the revisions in economic priorities brought about by induced change. Even though a bank's investment policy must be ultimately the result of decisions based on informed judgment rather than on any set rules and procedure, one could lay down certain broad principles which must underlie the banker's decisions. These general principles are :

(i) *Safety.* The principle of safety must be the primary principle. Advances made, and securities purchased, must be such as not to involve the funds of the bank to any risks of being lost. It must, however, be recognised that safety as a criterion is essentially a relative concept, referring as it does to an assumption of normal economic and business conditions continuing. In a sense, the application of the principle of safety is a negative one emphasising that

(a) *prima facie* unsafe loans should be avoided, and

(b) as between equally profitable investments, the more safe one should be preferred.

(ii) *Maturity spread-over.* Since liquidity for a bank must mean ability to meet demands at all times, investments of the bank must not involve locking up of funds for periods and amounts which reduce liquidity to a margin below the requirements for maintaining encashability of demands. This really implies that various investments must be held in such a manner as to more or less coincide as regards

maturity with the borrowings of the bank. Normally, a commercial bank obtains its funds for short (at best medium) periods. Thus, a commercial bank's liabilities being repayble on demand or at short notice, it can lend funds only for a short period. Further, commercial banks must always be in a position to shorten the maturity of their holdings, and, recall, if necessary, loans made to meet the demands of its depositors in case of a general withdrawal of the deposits from the bank ; hence, the importance of the item "money at call and short notice."

(iii) *Wide dispersal of borrowers.* It is usually preferable to advance moderate sums to a large number of customers than to lend large amounts to a small number. This principle is based on the simple law of probability that there is always a less chance of there being a general default by many customers. The principle may be further extended to cover the idea of avoiding concentration of loans on a few lines of business, especially if they are interlocked and mutually dependant for prosperity, as depression in particular lines of production is less unavoidable than a general depression of the entire economy. In simple language all this only implies that a bank should not invest all in eggs nor put all the eggs it has in the same basket.

(iv) *Profitability.* However much the term 'profit' may be at a discount in a socialistic pattern of economy, banks must and should make profits. The income of banks must be, at least, sufficient to pay an adequate rate of interest to attract deposits and meet its costs of operation. One of the paradoxes in India is the reluctance to stimulate savings by making it attractive to save. Thus, we have the Reserve Bank directing scheduled banks "not to pay interest at a rate higher than 2 percent below the Bank rate on deposits repayable on the expiry of a period not exceeding 21 days from the date of deposit or on notice of not more than 21 days"; we also have a virtuous indignation against any normal and long period rise in deposit rates as it may "increase borrowing costs and endanger plan targets." We do not, however, seem to recognise that if domestic savings must be stimulated, an increased rate of savings can normally follow only from a more attractive deposit rate; and, that only if the banks

have more funds would they be able to extend their investments to more profitable fields and simultaneously aid productive effort according to the objectives of the plan. However, a banker should recognise that an investment which has a higher profitability because it is more risky, is an illusory attraction and is best avoided in the interests of prudent banking.

(v) *Mixed holding of Government Securities, Stocks and Shares.* Usually all banks have a fairly large portfolio of securities. Investment in securities is more convenient than extending loans and advances or discounting bills, and there is a tendency in the banking system to lay increasing emphasis on this form of invesment. The advantages claimed for investing funds in securities are :

(a) quick marketability,

(b) steady yield,

(c) comparatively greater safety, and,

(d) absence of violent fluctuations in price.

These are undoubtedly substantial advantages, but it would be obviously incorrect to assume that all types of securities satisfy all the conditions outlined above. For example, Government securities are safe, easily marketable and provide a steady return, but their value would alter with changes in the Bank rate or with revisions in the rates of interest offered for new floatations. They would suffer capital depreciation with a rise in long term rates of interest. Industrial stocks and shares on the other hand may yield a more profitable rate of return, though their yield may be variable ; but, it cannot be claimed that they are as safe as giltedged government paper, though dealing in "blue chips" has lately been quite fashionable. A bank's portfolio of securities has, therefore, to be a mixed lot. It must be made up of a judicious mixture so as to ensure all the qualities being satisfied for the 'bag' as a whole, though particular lots may suffer from one or other of the shortcomings.

To sum up, we find that the structure of assets or pattern of investment for the banking system is a complex affair. No simple straightforward rules can be laid down for achieving an ideal distribution. Broadly, however, one might say that the banks must primarily aim at liquidity in their investment policy, for ability to command cash quickly is essential to meet an emergency, and, for a bank there is no such thing as ultimate solvency with short period inability to

meet demands, however abnormal or unjustified they may be. Liquidity for individual banks is generally much greater than for the banking system as a whole, for obviously each bank provides a support to every other bank while for the banking system there is no support beyond the Central Bank as the "lender in the last resort". Thus, while it is true that "the banking system is less vulnerable and more stable if the individual banks are in a genuinely liquid condition", it is also equally true that "there is no such thing as liquidity for the banking system as a whole". This is so because liquidity is dependant on marketability or shiftability, and for the banking system as a whole there are, in this respect, well-marked limits. The truth of this would be apparent when one recognises that :

> "An individual bank can dispose of its assets to the public or to another bank ; all banks taken together can shift them within the limits of law and practice to the Central Bank, if one is in existence. In certain circumstances, the banking system of a country may be able to invoke the aid of foreign banking systems for the same purpose...... ......(But) If every bank were to decline to renew its loans or to endeavour to place on the market its assets on any substantial scale, a complete breakdown of the economic system could be the only result."[151]

In reality, however, these limits are practically sufficient.

4·4 *Investment Pattern of the Banking System in India.* So far we have been considering the theoretical aspects of investment policy and have been trying to understand the considerations that underlie a proper approach to the distribution of assets. It would be interesting now to analyse the position as it actually exists in India. For purposes of this study, it would be desirable to analyse the behaviour of Indian Scheduled Banks and Foreign Banks seperately as here are wide differences between the two.*

Even a cursory glance at the table on next page brings out the very large investments held in Government securities. The peak holding was reached in 1959-60, since when there is a definite trend towards a decline in Government securities held, with an increase in bank credit. The ratio of Government securities to total liabilities of 32% in 1961-62 was

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151. Muranjan, S. K.—Modern Banking in India, p. 187.

* Non-Scheduled banks have limited total operations and require no detailed study.

Indian Scheduled Banks
(Business in India)

(Amount in lakhs of Rs.)

Year (Average of Fridays)	Balances with other banks in current account	Investments in Government Securities	Money at call and Short notice	Total Bank Credit	Percentage to aggregate liabitities of Column (3)	Percentage to aggregate liabitities of Column (5)
(1)	(2)	(3)	(4)	(5)	(6)	(7)
1951-52	9,43	257,08	4,20	405,44	37·37	58·94
1955-56	9,08	322,63	8,98	466,23	39·75	57·44
1956-57	9,06	316,49	9,16	585,01	34·91	64·53
1957-58	9,53	344,00	23,45	685,37	31·04	61·85
1958-59	11,41	521,15	33,55	721,08	38·83	53·72
1959-60	13,22	680,86	18,54	807,31	43·37	51·42
1960-61	14,54	647,25	13,11	952,73	38·55	56·74
1961-62	14,91	542,39	31,12	1,054,39	32·00	62·21

Source : R.B.I

N.B. 1. For aggregate liabilities, See table in para 3·4·2.

2. Column (5) includes
   (i) Loans, Cash Credits and overdrafts
   (ii) Bills purchased, inland and foreign
   (iii) Advances due from Banks.

practically the lowest, being only slightly higher than the record low figure of 31·04% reached in 1957-58. It is a debatable proposition as to whether the steady decline in the ratio of Government securities to total liabilities, as is obviously the trend for Indian Scheduled banks, is a desirable one or not. In a sense it shows more progressive banking, for fundamentally the function of a bank is creation of bank credit. It may, however, involve increasing pressure on the Reserve Bank of India and non-bank institutional investors in India (*e.g.* General Insurance Companies, the S.T.C, the Life Insurance Corporation, Industrial Finance Corporation and the like) who may gradually have to hold more and more of Government securities since the Public Debt of India must continuously increase due to requirements of planning. It must, however, be noted that the high level of holding of Government securities is not peculiar to India ; it is a widely observed feature of banking in many parts of the world, including countries which are far more developed in all respects than India is at present.

Foreign Banks
(Business in India)

(Amount in lakhs of Rs.)

Year (Average of (Fridays)	Balances with other banks in current account	Investment in Government Securities	Money at call and Short notice	Total Bank Credit	Percentage to aggregate liabilities of Column (3)	Column (5)
(1)	(2)	(3)	(4)	(5)	(6)	(7)
1951-52	2,44	46,66	7,19	141,98	27·24	82·88
1955-56	1,67	48,08	6,64	166,24	25·06	86·63
1956-57	1,45	42,86	3,95	196,63	22·76	104·40
1957-58	1,52	40,65	11,46	205,43	19·49	98·48
1958-59	1,49	43,75	14,58	178,09	21·17	86·19
1959-60	1,50	43,79	13,60	180,18	20·20	83·13
1960-61	1,54	40,70	15,68	207,47	17·25	87·93
1961-62	1,54	42,62	13,78	232,87	16·60	90·71

Source : R.B.I.

N.B. 1. For aggregate liabilitities, see table in para 3·4·2.
2. Column (5) includes
(i) Loans, Cash credits and overdrafts,
(ii) Bills purchased, inland and foreign
(iii) Advances due from banks.

A comparison of the trends revealed by the above table with those relating to Indian scheduled banks would show that the holdings of Government securities by the foreign banks works out to a much lower percentage in terms of their total liabilities. In fact the policy of these banks appears to be to concentrate on bank credit* in accordance with the normal and well-established traditions of modern western banking. Another interesting feature that may be noted is that the variability in absolute holdings of Government securities is much less in the case of foreign banks than in the case of Indian banks. This is partly due obviously to the lower total holdings of foreign banks ; but, mainly it is the result of a policy of using bank credits as the primary shock absorber of variations in aggregate liabilities.

5. Bank Deposits in India.

5·1 *An Analytical Distinction.* We have seen that bank deposits may be passively or actively created, but that it is

* The student reader may try to find out for himself the explanation for the peculiar figure in column 7 for 1956-57, and also why the sum total of columns 6 and 7 exceed 100 in this table.

difficult to analyse from available existing data the exact proportions of deposits emanating from credit operations through granting of loans and advances and those resulting from positive acts of savings. In a sense the distinction is really not so clear-cut as it may appear at first sight. Banking is a continuous and simultaneous operation in which banks are either creating deposits for value received or bringing them into existence against promises to repay in future. The two sets of forces bringing into existence passive deposits and actively created deposits are continually in operation affecting the aggregate volume of deposits for the banking system as a whole. It must be recognised that the types of deposits are very much interrelated. Every actively created deposit increase the demand for withdrawal from a bank, for obviously loans and advances are taken with the intention of their being utilised. However, a withdrawal from a given bank is not necessarily a withdrawal from the banking system in the sense of conversion of bank credit into currency. A withdrawal from one bank, in an economy where banking is fairly developed, is, in course of time, an effective passive deposit for another bank, or, sometimes an effective passive deposit in the same bank by another customer. Thus, a banking system works by

(a) creating active deposits on the basis of resources made available by passively created deposits, and

(b) having its resources augmented by some of the actively created deposits returning to it in the form of passively created deposits.

Of course, the banking system cannot, so to say, feed itself indefinitely by actively creating deposits. The needs of cash reserves to meet requirements of payments made accordingly, and differential redistribution of resources following from credit creation compelling some banks to step backwards because their cash reserve-ratios are becoming deficient, would provide a check to aggregate expansion of bank credit with given volumes of value tendered in the form of net savings leading to passive deposits. It would, however, have been interesting to study the relative movements of the two types of deposits, both compared to each other and compared to the aggregate volume of deposits as a whole, if statistical data were available in appropriate form. In actual practice we have information only relating to demand-deposits and time-deposits. It has already been pointed out that neither could be accurately treated as synonymous fully with the concepts of actively created or passively created deposits. However, *prima facie* (and very imperfectly) one could regard time-deposits as mainly due to savings and demand-deposits

as mainly due to loans and advances, though even such a broad statement is subject to analytical limitations.*

5·2 *A Factual Study.* The classification of deposits into time-deposits and demand-deposits is important from two points of view. First, it enables us to get some idea (in a very limited and imperfect way, of course) of the nature of resource creation by the banking system. Secondly, it is a good basis for examining the adequacy or otherwise of reserve-ratios maintained, for the withdrawability of demand-deposits being greater, a given cash reserve-ratio may be inadequate if total liabilities remain constant but the proportion of time-liabilities decreases. However, the cash reserve-ratio is in terms of the aggregate, and the only minor recognition given to the distinction is the statutory provision of the Reserve Bank of India which enables it to vary the minimum cash reserves maintained with it from 2 to 8 percent in respect of time liabilities and 5 to 20 percent in the case of demand-liabilities.

All Scheduled Banks(1)

(In lakhs of rupees)

		No. of reporting Banks(1)	Liabilities Demand	Time	Total	Cash in hand (Notes and Coins)	Balances with Reserve Bank	Cols. (6+7) as per cent of Col (5)
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
	Last Friday Figures							
1951	,,	94	553,25	289,71	842,96	43,25	45,75	10·56
1955	,,	89	615,60	412,62	1,028,22	39,33	60,88	9·75
1956	,,	89	643,37	457,16	·1,00,73	38,55	51,98	8·22
1957	,,	91	701,82	665,69	1,367,51	39,63	67,88	7·86
1958	,,	93	693,96	897,57	1,573,53	43,32	76,01	7·58
1959	,,	94	716,87	1,110,22	1,827,09	44,52	69,53	6·24
1960	,,	94	745,51	1,093,96	1,828,51	51,74	110,10	8·86
1961	,,	94	773,61	1,094,90	1,828,51	51,74	110,10	8·85
Jan. 1962	,,	83	795,75	1,136,20	1,931,95	46,71	79,13	8·02

Source : R.B.I.

N.B. 1. Liabilities exclude borrowings from Banks and inter-bank deposits.

2. Last Friday figures have been taken instead of average of Friday figures in this table because liquidity must be maintained at each point of time.

* See earlier, para 2·2·4.

We find that a trend towards lower reserve-ratios took place in the period 1956 to 1959, but that this has been halted and the reserve ratios seem to have more or less stabilised during the last three years at a figure slightly lower than what operated at the end of the First Five Year Plan.

6. Commercial Banking in India.

6·1 *Components of Commercial Banking.* In the category of commercial banks, we include in India the following :—

(i) The Indian Joint Stock Banks,

(ii) The Exchange Banks, *i.e.* branches in India of banks in foreign countries,

(iii) The State Bank of India.

The different banks are classified by the Reserve Bank of India as scheduled banks or non scheduled banks. All commercial banks perform the normal functions of banking (see para 1·3), but the exchange banks concentrate more on the financing of India's foreign trade while the Indian commercial banks prefer to devote greater attention to internal trade and commerce. Fundamentally, of course, both Foreign (exchange) banks and Indian commercial banks perform the same type of functions and have similar tendencies, more or less, on broad banking features, but in view of their differing organisation, and interests, it is best to consider their problems separately. The State Bank of India, which was formerly the Imperial Bank of India, formed by merging the three Presidency Banks in 1921, has a peculiar position in the Indian banking system. It has, no doubt, lost its position as the acknowledged head of the Indian banking system since the establishment of the Reserve Bank of India in 1935, but it continues to be different from the other commercial banks because it still retains certain privileges. The State Bank of India occupies a place of importance not only because it is a nationalised undertaking in the public sector but also because it conducts Government business and acts on behalf of the Reserve Bank where the latter has no offices of its own. The State Bank of India, therefore, enjoys both the prestige of antiquity (dating as it does from the days of the Presidency Banks which derived their authority under the Presidency Banks Act of 1876) and of official dignity derived from acting as bankers handling Government funds.

6 2 *Scheduled and Non-Scheduled Banks.* The distinction between these two categories of banks is important. The origin of the distinction is to be traced to the inauguration of the Reserve Bank, which, in accordance with the

statutory provisions of the Reserve Bank Act, divided joint stock banks in India into two main classes, namely, scheduled banks and non-scheduled banks. Broadly speaking, scheduled banks are similar in conception, though not identical in every respect, to what are called 'member banks' in U.K. and U.S.A. Literally, scheduled banks are simply those institutions which are included in the second schedule to the Reserve Bank Act, while those not so included, but performing recognised banking functions, are termed non-scheduled banks. The distinction is both important and paradoxical. It is important in the sense that scheduled banks have specified relations with the Reserve Bank and, to the unwary public at least, they appear to have a higher status in the banking system. The distinction, however, is paradoxical in the sense that it is neither an index of greater safety or efficiency, nor does it impose on the Reserve Bank any obligation that scheduling as such provides an assurance that such a bank in difficulties will receive assistance as a matter of course.

6·2·1 *Conditions of Scheduling*. A bank must fulfil certain conditions before it can be classed as a scheduled bank. These conditions are laid down in section 42(6) of the Reserve Bank Act, and, are

(i) it must be a company or a corporation under appropriate law,

(ii) it must have a paid-up capital and reserve of an aggregate value of not less than five lakhs of rupees,

(iii) it undertakes banking business,

(iv) its inclusion must be directed by the Central Government through a notification in the Gazette of India.

It is obvious that the scheduled banks must form a rather heterogeneous group for the banks satisfying the above conditions would vary widely in economic strength, public confidence, period of existence and extent of business. For instance, it would include on the one extreme the State Bank of India with its enormous resources and privileged position, and on the other extreme we would have recently established institutions with capital and reserve amounting to just a little over Rs. 5 lakhs. In between there would be a variety of banks like the Exchange Banks which are branches of large institutions incorporated outside India, the big Indian banks with a network of branches, and medium sized banks with limited range of activities. The position, therefore, is rather peculiar. The law recognises Rs. one lakh as the minimum capital and reserve for being recognised as a bank, and yet another law distinguishes between them for purposes of scheduling to the Reserve Bank. Finally, scheduling is not

a permanent 'privilege' ; the Reserve Bank Act provides that banks are liable to be excluded from the schedule if the value of their capital and reserves falls below the prescribed minimum or if they go into liquidation or otherwise cease to carry on banking business.

6·2·2 *Relations of Scheduled Banks with Reserve Bank.* Certain facilities are available to scheduled banks under the Reserve Bank Act. The most important facility which these banks enjoy is that of financial accommodation in the shape of the rediscount of eligible bills or loans and advances against eligible securities from the Reserve Bank. Such facility, however, is not automatic, and a scheduled bank has to make itself eligible for such aid by demonstrating its soundness and stability satisfactorily. Thus, subject to the legal right on the part of the Reserve Bank to refuse, at its discretion, to rediscount the paper of any particular bank without assigning a reason, scheduled banks run on sound lines may always expect to receive ready assistance from the Reserve Bank if they can offer suitable security.

6·2·3 *Obligations of Scheduled Banks.* These banks have certain obligations under the Reserve Bank Act. These are :

(i) maintaining with the Reserve Bank a balance of not less than 5 percent of its demand and 2 percent of its time liabilities,

(ii) submission of weekly returns in prescribed form.

We have seen that recent legislation has empowered the Reserve Bank to raise, within limits, the minimum reserve ratios prescribed under (i) above, though its right to impose penal interest at prescribed rates in the event of failure to maintain the minimum statutory reserve has been incorporated from the very beginning in the Reserve Bank Act itself.

6·2·4 *Scheduling—a privilege ?* In what sense is it a privilege or a basic advantage to be included in the list of scheduled banks ? It is obviously not greater safety, for the inclusion of a bank in the schedule does not give any continuing guarantee of its soundness or stability. In fact, even scheduled banks have been compelled to close their doors. We have seen that Reserve Bank accommodation is not available, *ipso facto*, to a scheduled bank. On the other hand, various obligations are imposed on them which not only involve time, labour and expense, but may even impose some loss, *e.g.*, if the statutory minimum reserves maintained with the Reserve Bank are in addition to, and not a part of, the reserve it is accustomed normally to maintain. What then is the real advantage to the bank for getting itself scheduled ?

The position has been succinctly put as follows :

> "The advantage it gains really lies in its prestige in the public mind. Although a part of the prestige is ascribable to quite erroneous beliefs on the part of the public about the implications of scheduling, it cannot be denied that affiliation to the Reserve Bank carries an assurance that the bank is at least in outward conformity with the law and accepted decencies of the banking business."[152]

This, however, is a very unsatisfactory situation. Legally, the Reserve Bank does not take the responsibility of ensuring competent management ; nor, does it guarantee solvency of the scheduled banks. And yet, the Reserve Bank itself is continuously creating the impression that scheduled banks are somewhat different from others. It is difficult to believe that the Reserve Bank is unaware of the prestige value attached to scheduling, and, it seems to be unconsciously aiding in the creation and maintenance of an illusion.

7. Indian Joint Stock Banks.

7·1 *Meaning*. Though strictly speaking the State Bank of India should also be included in this category, because of its special position it would be convenient to study it separately. Basically, the Indian joint stock banks are those registered under the Indian Companies Act which had adopted the rather crude definition of a banking company as that "which carries on as its principal business the accepting of deposits of money on current account or otherwise, subject to withdrawal by cheques, draft or order." We have seen earlier that the concept of banking is best linked to its functions, particularly that of a dealer in credits with borrowed funds. Thus it is not surprising that the definition of a banking company was made more precise in the Banking Companies Act of 1949 which adopted the following definition of banking :

> "the accepting for the purpose of lending or investment of deposits of money from the public, repayable on demand or otherwise, and withdrawal by cheque, draft, order or otherwise."

Of course, even this definition is not scientific enough nor complete enough, though it does bring out more emphatically the peculiar nature of the sources of a commercial bank's business funds.

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152. Muranjan, S. K.—Modern Banking in India, p. 279.

7·2 *Functions.* Being commercial banks, the Indian Joint Stock Banks perform all the functions which are expected of them, *viz,.*

(i) accept deposits,
(ii) grant loans and advances,
(iii) discount bills,
(iv) remit money from place to place,
(v) purchase and sell securities on behalf of their clients, and
(vi) provide safe-custody facilities.

7·3 *Development.* Growth of banking is to be judged by the services rendered. The lending operations of these banks depend to a very great extent on the resources which they can secure by attracting deposits from people who have money to spare for the time being, or by obtaining loans against their investments of various categories. The resources available from share capital and reserves are also there, but these generally do not provide much funds. The growth of these resources are indicated in the following table :

Indian Scheduled Banks

(Rs. Lakhs)

Year (Last Friday)	Paid-up Capital	Reserves	Aggregate Deposits	Number of Reporting Banks
(1)	(2)	(3)	(4)	(5)
1951-52	33,50	26,91	632,93	76
1955-56	32,53	28,12	814,96	71
1958-59	35,79	33,30	1,386,24	78
1959-60	36,21	32,65	1,614,43	78
1960-61	36,52	32,27	1,586,66	74

Source : Reserve Bank.

Analysis of the above figures show that apart from growth of deposits, there is very little other evidence of expansion of banking. It is, of course, a good thing that unnecessary multiplication of small-sized banks has been practically stopped, so that basically the larger aggregate deposits show an increase in the average deposit per reporting bank (the total number of which in 1951-52 was 76, 1959-60 it was 78 and in 1960-61 it fell to 74). However, it is also equally

clear that increasing deposits were more the results of inflationary trends than outcome of mobilisation of resources, and it is by no means certain that greater mobilisation of resources would not have taken place if there was a deeper infiltration of banking in untapped areas.

Compared to rather phenomenal growth of the scheduled banks, the progress of non-scheduled banks was very limited as is revealed from the following figures :

Non-Scheduled Banks

(In Rs. Lakhs)

Year	Paid-up Capital	Reserves	Aggregate Deposits	Number of Reporting Banks
(1)	(2)	(3)	(4)	(5)
1951-52	6,46	2,17	39,04	442
1955-56	7,94	4,30	62,22	378
1958-59	5,59	3,12	46,56	279
1959-60	4,99	2,93	48,43	267
1960-61	4,72	2,77	48,44	256

Source : R.B.I.

In spite of relatively low figures of deposits, there is a redeeming feature, *viz*, increase in the average per bank deposit. Further, the substantial decline in the number of non-scheduled banks is probably a move in the right direction and represents a desirable trend in Indian banking.

7·4 *Expansion of Facilities.* Efficient banking from a national point of view means the spreading of facilities and making available the advantages of banking to more extensive areas, particular at those places where previously no banking facilities existed. It is undoubtedly true that the number of offices of Indian joint stock banks has increased substantially during the last few years ; but, it must be recognised that there is an unfortunate tendency amongst Indian banks to "herd together", so that there is usually an intensive increase of banking facilities made available in the same areas rather than an extensive spreading of banking in remote and interior places. However, there is no doubt that extension of facilities has taken place as is revealed by the following figures.

Number of Offices of Banks

Year	Indian Scheduled banks	Non-Scheduled banks
1951-52	2,226	1,460
1955-56	2,345	1,204
1958-59	2,897	890
1959-60	3,087	866
1960-61	3,186	827
1961-62	3,410	692

Source: R.B.I.

7 5 *Ownership Pattern of Deposits.* Unfortunately, no detailed information spreading over a number of years with comparable concepts and definitions is available on this very important feature of banking. However, recently a survey has attempted to get some information on this aspect, and, the meagre information available indicates the following position :

Category of holder	Percentage of deposit held of Demand Deposits	Time Deposits	Savings Deposits
(1)	(2)	(3)	(4)
1. Manufacturing, financial and other business concerns	50	19	N. A.
2. Government and Quasi-Government bodies	11·6	10·5	N. A.
3. Individuals (*i.e.* personal deposits)	21·8	35·4	85·6
5. Undefined	...	...	...

N. B. 1. Figures are rounded
2. Grouping arrived at in broad categories
3. Undefined = remainder
4. N. A. = negligible or not available.

The information revealed by the above table is admittedly very meagre and unsatisfactory, and, can give, at best, only broad dimensional ideas.

7·6 *Assessment.* There is no denying the fact that Indian joint stock banks have contributed substantially to the economic life of India. It would be unfortunate if one were to regard a casual bank-failure here or there as a basis of wholesale condemnation of Indian banking as such. If indi-

vidual cases of bank-failure are critically examined, it would appear that in most cases they were the result of inefficient and undesirable managment because of the influence of particular individuals. Such cases do not prove that, by and large, the management of banking in India is not prudent. However, to say that broadly the working of the Indian joint stock banks has been in accordance with the broad objectives of banking is not to say that in particular respects there have been no shortcomings. It would, therefore, be useful to enumerate the more important criticisms that have been advanced against Indian joint stock banks and to examine how far they are justified.

7·6·1 *Examination of Criticisms.* The following are some of the more important defects that have been pointed out :

(a) *Unbalanced geographical spread.* It has been stated earlier that there is a tendency amongst Indian joint stock banks to pursue one another and concentrate their activities in urban areas, particularly the more thickly populated cities and towns. The result has been that the State-wise development of banking in India has been unbalanced,* It must, however, be recognised that the nature of the activities of commercial banks are such that they are hardly likely to extend their activities to rural areas, where banking facilities must continue to be provided for a long time to come by the post-office savings banks and the co-operative banks. Even then it does seem possible to spread banking a little more to the borderline areas, especially as the extension of the monetized sector and the growth of all-India markets for agricultural products are steadily linking the rural areas with urban areas in regard to monetary transactions.

(b) *Diversion of capital from less developed areas to areas with more profitable investments.* This, to be quite frank, is really not a criticism of commercial banking but an expression of narrow regionalism. The criticism takes the form of a complaint that the deposits collected at the branch offices at mofussil centres are diverted to head offices for investment in other centres at rates of interest more favourable than those obtainable at the place where the money is collected. It is obvious that the essence of the development of branch banking is to raise capital from wherever savings are available and to utilise it most profitably consistent with safety.

* See Vol. I. p. 65,

It can be no part of the functions of a bank to bring into existence profitable uses of capital. It confines itself to the role of making capital available if there is an economic demand for it, distributing the scarce available resources according to productivity. In fact, such a policy is more consistent with the best economic use of national resources than any policy of local demarcation of uses of local savings could be.

(c) *Rising costs of bank services.* Some rise of costs is inevitable in an inflationary economy, especially when national labour policy is continuously directed towards 'pay-awards' to compensate the moderately paid employee against rises in cost of living. To the extent, therefore, rise in bank costs has been the result of the unavoidable effects of general rise in costs all round, there is hardly any justifiable reason to complain. It has, however, been sometimes argued that there has been a fall in efficiency since a steady increase in the number of officers needed to supervise and control the assets of banks in India is noticeable with increasing deposits. Banking is an industry where overhead supervisory costs should not rise proportionately with rise of business, and after a certain level of supervisory organization has been reached, it should remain constant, if not decline per given quantum of assets. In the U. S. A., for instance, it has been calculated that the average number of officers and supervisors needed for assets of \$ 1 million remained practically constant during the decade 1950-60, being approximately 2·3 throughout. In India, on the other hand, the average corresponding figure rose during the same period for each Rs. 1 Lakh assets from 1·5 in 1955 to 1·9 in 1959.* Thus the costs of banking services in India has not only been rising, even absolutely it is nearly 40 times as high. International comparisons are, of course, subject to serious limitations, but even then, there is no denying that banking is an expensive industry in our country for the nation as a whole.

(d) *Absence of a close relationship between banks and their customers.* It has been pointed out in various connections that in India there is :

(i) an absence of touch and lack of knowledge resulting therefrom between borrowers and lenders, *i.e.* between banks and their customers,

* See Vol. I, p. 104, for estimates of employment in banks.

(ii) an absence of the healthy western practice of 'one man, one bank'.

To a certain extent, these tendencies are inherent in a baninkg system where the average size of the unit of effective operation is on the rise; partly, these also are the logical corollaries of the growth of branch banking with a transferable cadre of officers in a country where differences of language and social environment are sufficiently great to prevent quick absorption of a new person in the social life of a community. Whatever the cause, there is no doubt that impersonal relations between a banker and his client does not lead to efficient banking in the long run, for intimate knowledge of the borrowing customer is essential for sound banking, especially as there are no organised agencies for supplying information concerning the financial standing of borrowers.

7·6·2 *Leading Achievements*. In a sense, the last decade has brought about a basic change in the outlook of the Indian joint stock banks. The old spirit of unhealthy competitive rivalry has been on the decline and progressive action by voluntary agreement is on the increase. The most important step taken in this respect was Deposit Rate Agreement whereby banks reached, on a voluntary basis, an agreement on the structure of rates on deposits. This agreement was a welcome evidence of the desire of banks to enforce self-discipline. Secondly, one notices during the last decade a desire on the part of Indian joint stock banks to fall in line more readily, on a voluntary basis, with planning policies of the Government. It is true that to a certain extent such co-operation was making a virtue out of necessity for as planned control spreads, allocations of credit by banks have to follow the lines of Government policy. Even then, however, things were made easier for planning, since a willing horse, even when willing because of the bridle and the stirrup, is always a more convenient agency for forward movement. Finally, there has been a progressive rise in the standard of banking throughout the country contributing to the increasing protection of the interests of the public and particularly of the depositors, so that safe banking to-day is increasingly the contribution of better bankers rather than more rigid laws.

8. Exchange Banks.

8·1 *Definition and Concept*. Exchange banks may be defined as banks with head offices outside of India, having their capital in other currencies than in rupees. Historically, these banks are the oldest ingredients of the Indian banking system, and, have done probably more for the development of banking in this country than is generally recognised. They are a part of commercial banking of the country and are

included in the Reserve Bank of India's category of scheduled banks. In statistical classification they are termed as "Foreign banks" and since detailed data is available regarding their activities, an appraisal of their functioning in the banking system of the country is fairly easy.

8·2 *Functions.* The earlier importance of the exchange banks lay in their role as financiers of

(i) India's foreign trade—both exports and imports, and,

(ii) the internal trade from port to the consuming centre and from production centres to the ports.

These aspects of the work of the exchange banks were very important, and, prior to the inauguration of the era of planning, significant for the economic prosperity of the country. With the development of planning on the one hand, and the growth of import control and exchange control on the other hand, the initiative and role of the exchange banks in the field of foreign trade finance is apparently on the decline. Further, with the adoption of export promotion as a national policy, together with the establishment of specialized agencies for assisting in exports, the scope for unregulated foreign trade finance is a dying function.

The exchange banks have also always performed the ordinary banking functions of accepting deposits, discounting bills and making advances to trades, industry and commerce. In this respect they have always been competitors of Indian joint stock banks, and the severity of their competition in this field of business, always great, has been naturally on the increase with the decline in the quantum of their foreign trade finance ; since their discretion and freedom to conduct foreign trade financing business in their own way has been severely curtailed in recent times (not through any discriminatory measures against them but because of the general growth of control and regulation in the field of foreign trade payments) they have naturally given more attention to their general banking functions with the inevitable effect of intensifying further competition with Indian joint stock banks.

8·3 *Exchange Banks and Financing of Foreign Trade.* A favourite topic for grumbling, and a controversial topic which, more often than not, generated much heat was the alleged anti-Indian practices that the exchange banks were said to have followed in the matter of financing of foreign trade. However, both the procedure for such financing and its objectionable features[153] are now, at best, parts of a histori-

153. The student reader may find it necessary to know something about these ; See, Report of the Indian Central Banking Enquiry Committee paras 427—446.

cal narrative with little practical significance. Today, foreign trade is largely controlled and circumscribed ; command over foreign exchange is severely limited ; in short, the bankers role in determining preferential allocation of benefits of finance in the field of foreign trade is practically non existent and would be more so with the growth of bilateralism in trade and agreements for rupee payments for imports. There is, therefore, not much point in even examining the old allegation against the exchange banks in this respect, especially as these banks are now as much a part of India's normal commercial banking as the Indian joint stock banks are.

8·4 *Status of Foreign Banks.* Technically, these banks are a part of the recognised commercial banking system and are subject to practically the same regulation from the Reserve Bank of India as their Indian counterparts. There are few privileges left to the exchange banks, and even those that continue legally are more formal than real, for regulatory control through the "Laws" in India is seldom onerous. As the Reserve Bank of India is now in a position to collect and collate figures relating to their business in India, whatever difficulties existed earlier as to the ascertainment of their business interests in India has been removed. The exchange banks are all listed as scheduled banks, and, their relationship with the Reserve Bank of India is similar to other scheduled banks and is governed by a uniform policy. It is true that the exchange banks still command great public confidence partly because of past history and partly because of an assumption (not unreal) of greater safety, so that in any open field of competitive business they are likely to be at an advantage over their Indian rivals : but such a position of advantage could hardly be an economic loss to the country as long as no anti-national or anti-social policies are pursued by them. Finally, as bankers to the average individual customer, the exchange banks are undoubtedly far more efficient, so that it is not surprising that the customer of limited means but accustomed to a slightly modernised version of banking facility should prefer the foreign banks.*

8·5 Development and Business of Foreign Banks in India.

8·5·1 *Numbers.* The number of foreign banks is extremely limited, being only 16, and their offices in India are also infinitesimally small compared to those of the Indian banks. The insignificant position of the foreign banks in

* An interesting paradox which many of us have experienced is the greater courtsey shown by Indian employees of foreign banks to their Indian customers than that shown by similar employees of Indian banks !

India in terms of number of offices is indicated in the table below :

Number of Offices of Banking Companies in India

Year (End of)	All Commercial Banks (3+8)	All Scheduled Banks (4+7)	Indian Scheduled Banks: Total	Indian Scheduled Banks: State Bank of India	Indian Scheduled Banks: Indian Joint Stock Banks	Foreign Banks	Non-Scheduled Banks
(1)	(2ı)	(3)	(4)	(5)	(6)	(7)	(8)
1950-51	4,149	2,689	2,624	398	2,226	65	1,460
19 5-56	4,102	2,898	2,831	486	2,345	67	1,204
1956-57	4,175	3,018	2,951	551	2,400	67	1,157
1957-58	4,349	3,393	3,324	644	2,680	69	956
1958-59	4,603	3,713	3,646	749	2,897	67	890
1959-60	4,862	3,996	3,928	841	3,087	68	866
1960-61	4,993	4,166	4,096	910	3,186	70	827
1961-62	5,135	4,443	4,366	956	3,410	77	692

Source : R.B.I.

8·5·2 *Development.* As has been pointed out earlier, one should look to the details of liabilities and assets of a bank to judge its true strength. So far as the foreign banks are concerned, it is not possible to get an allocated portion of paid-up capital for their business in India, but figures of reserves and aggregate deposits, being available, provide a fair index to their growth during the last decade.

Foreign Banks

(In Rs. Lakhs)

Year (Last Friday)	Reserves	Aggregate Deposits	Ratio of cash to aggregate deposits
(1)	(2)	(3)	(4)
1951-52	1,46	153,52	10·3
1955 56	3.35	174,65	7·2
1958-59	4,57	192,56	6·6
1959-60	4,69	219,16	7·3
1960-61	4,98	220,23	5·5

Source : R. B. I.

N. B. 1. Number of reporting banks 16, except for 1955—56 when it was 17; figures relate only to India.

2. Cash=Cash in hand plus Balances with Reserve Bank

3. Column 3=Demand deposits plus time-deposits, excluding Inter bank deposits of either type.

The information thrown up by the above table is instructive. It shows the rapid increase of their deposits, and since the number of banks remained constant, the average per bank deposit rose very fast. So far as their reserves are concerned, it cannot be said that it has grown adequately, though if one looks only superficially one would find that the percentage rate of growth is not unreasonably slow. Finally, since the majority of these banks are U.K. banks, the characteristic English banking practice of keeping a low cash reserve ratio is clearly noticeable. The low reserve-ratio, however, is not unusual because of their practice of keeping a higher proportion in the from of bank credit, particularly advances, and holding a lower proportion of Government securities. This is illustrated in the table given below :

Foreign Banks

Year (Last Friday)	Bank Credit: Advances	Bank Credit: Bills purchased and discounted	Bank Credit: Total	Investments: Total	Investments: Government Securities	Investments: Others	Percentage to aggregate deposits of (4)	Percentage to aggregate deposits of (5)
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
1951-52	154,41	4,93	159,34	45,97	44,70	1,27	103·8	29·9
1955-56	154,75	18,91	173,66	50,62	47,16	3,46	99·4	29·0
1958-59	146,17	21,42	167,59	45,38	43,25	2,13	87·0	23·6
1959-60	155,34	28,61	183,95	44,16	41,85	2,31	83·9	20·1
1960-61	189,35	30,88	220,23	41,21	40;46	75	100·0	18·7

Source : R. B. I.

The above table brings out clearly the greater significance of bank credit, particularly advances, in the investment policy of these banks, and, the comparatively minor role of Government securities. Strictly from a banking angle this is the proper investment policy, for the larger the proportion of Government securities handled by the public directly and purchased by it as forms of real net savings the, greater is the likely advantage from mobilisation of resources in an expanding economy.

8.6 *Appraisal and Assessment* 8·6·1 *Outlook* Even though exchange banks are, to all intents and purposes, full-fledged members of the Indian banking system, it seems necessary to investigate the question whether and what kind of dangers and eventually what advantages there are in the activities of foreign banks. The problem obviously is much different today than what it was prior to 15th August, 1947. As long as

India did not have a national government, one could hold the view that foreigen banks were probably in a position to undertake activities which were more likely to yield them profits and advantages to foreign trader, than promote the general interests of the economy of the country. The position today is naturally different as one can reasonably expect the Government of India and the Reserve Bank of India to ensure that nothing contrary to national interests is allowed to operate. In fact, even the foreign banks must recognise that it would not be to their own long period interest to undertake activities that would be frowned at by public opinion, for the government of an independent country must, sooner or later, take effective note of mounting adverse public opinion.

8·6·2 *Foreign Banks and the Law.* The provisions of the Banking Companies Act, 1949 are applicable to the exchange banks. The different provisions of this Act lay down the manner in which commercial banking generally is to operate and, those relating to licensing, restrictions on loans and advances, opening of branches, maintenance of case ratios, inspections etc. are applicable to both Indian joint stock banks and the exchange banks. There are also certain special restrictions which have been imposed on foreign banks, ostensibly with a view to safeguarding the interests of Indian depositors. The more important of these provisions are :

(a) banking companies incorporated outside India should have a minimum paid-up capital and reserves of Rs. 15 lakhs, and minimum of Rs. 20 lakhs if they have a place of business in Bombay or Calcutta,
(b) the first charge on the amount deposited with the Reserve Bank by a foreign bank would, in case of liquidation, be that of the Indian depositors and Indian creditors of the bank,
(c) foreign banks must prepare each year a statement of profit and loss and a balance-sheet in respect of business transacted in India,
(d) each foreign banking company will have assets of not less than 75 percent of its demand and time liabilities at the close of the last working day of each quarter.

None of these provisions are onerous. In fact, many of them are purely mechanical and have little effect on ensuring safety of the banks concerned. The first one, for instance, is discriminatory and attempts to enforce a higher minimum requirement for exchange banks, but is hardly of much practical significance for in practice these exchange banks (at least, those that matter) have much higher provisions in this respect.

In addition to such specific statutory provision, the real effective control over the exchange banks emanates from their being scheduled banks of the Reserve Bank of India. It would obviously be idle to expect the law to achieve qualitative improvement in the foreign banks if the Reserve Bank could not coerce them to a proper banking policy through its various powers of control and regulation.

8·6·3 *Efficiency achieved and competition provided.* In terms of adequacy of foreign trade finance provided, there has never been any doubt that the exchange banks have done a good job both in the past and to-day. Whether the use of Documents on Acceptance (D/A) for export trade and Documents on Payment (D/P) for import trade[154] was justified or not and whether there was an element of unfair discrimination against Indians in the relative choice, is, to-day, a moot point, for with regulated imports, assisted exports and exchange control such distinctions have ceased to have any practical significance. Further, there is little evidence to conclude that the exchange banks have neglected related aspects of inland trade in view of their highly specialised function of financing foreign trade. Finally, so far as efficiency is concerned, in terms of promptness, reliability and costs the exchange banks have been generally superior to the average Indian joint stock banks.

As regards competition provided by the exchange banks to Indian banks, it is clear that such competition is not, by itself, to be decried so long as there is no allegation of unfairness or corrupt practices.

In any case, in the field of foreign trade finance, Indian banks need have no worry about such competition, especially now, as long as they are not actively extending their activities into this field ; and, even if they were, as long as they have enough business for their funds, there can be little justifiable basis for criticising the exchange banks for providing a service that requires large capital and international connections. There is, however, one field in which a possibility of competition exists which Indian banks may have cause to fear. The exchange banks have very high prestige in India ; their goodwill is enormous and public confidence in their safety is so great as to enable them, perhaps, to raise deposits at cheaper rates. It could be argued, by stretching rather liberally the argument of 'infant' protection, that to the extent the exchange banks are able to use Indian capital, raised at lower

154. See Banking in the British Commonwealth—edited by R. S. Sayers pp. 152-54.

rates of interest, for snatching away business in the sphere of domestic trade from the Indian banks, there could be a grievance which was not quite illegitimate However, in fact, the deposits of exchange banks have shown no special tendency to rise faster than that of the bigger Indian joint stock banks, and, what is more important practically, the recent Deposit Rate Agreement takes away any preferential deposit-rate offering policy from the banks. Theoretically, however, the exchange banks could attract a larger volume of deposits at the same rates than their competitors, but that is a situation implicit in their position in the country from a purely banking angle and could hardly be the basis for discriminatory action against them, especially as there is no evidence to justify the allegation that Indian funds are to day also being used to benefit non-Indian business interests against their Indian rivals.

8·6·4 *Conclusion*. The exchange banks have a valuable part to play in the Indian banking system, especially so long as Indian banks are not able to establish sufficient numbers of foreign branches. Foreign branches are not an easy proposition nor an economic one at present due to foreign exchange difficulties. Indian banks are as yet not in a position to surmount such difficulties by attracting sufficient foreign deposits at their foreign branches, at least not in the more developed financial centres of the world. There is, therefore, no reason why we should not take full advantage of these foreign banks which have the resources of some of the strongest banks in the world, with widespread international connections and a net work of branches all the world over, especially as with a nationalised central bank in the form of the Reserve Bank of India we should have no difficulties in regulating their activities in the national interest.

9. The State Bank of India.

9·1 *Origin and establishment*. The State Bank of India was constituted on 1st July, 1955 under the State Bank of India Act 1955. It took over the Imperial Bank of India which was established in 1921 by amalgamating the three Presidency Banks. The Imperial Bank was not only the biggest commercial bank in the country between 1921 and 1955, but it also held, by virtue of its special functions and privileges, an unique status in the banking system. It performed :

(i) the ordinary functions of commercial banks,

(ii) the function of managing Government business, including holding of its balances,

(iii) partially the duties of a central banking institution as it

(a) managed the currency,

(b) regulated money market rates,

(c) performed clearing house functions,

(d) held the deposits of other commercial banks,

(iv) the duties of being the uncrowned head of the banking system as business houses, commercial banks and individuals applied to the Imperial Bank of India for loans and advances and rediscounting facilities.

The original Act imposed certain restrictions on the Imperial Bank's functions, *e g.*, it was not allowed to make loans for periods exceeding six months, it could not grant advances on the basis of immovable property and it was debarred from dealing in foreign exchange business. These restrictions were, however, removed by the Imperial Bank of India Amendment Act, 1934.

The real source of power of the Imperial Bank flew from its connection with Government and the facility it had from using Government balances which gave to it enormous liquid funds free of interest. Further, popular opinion regarded it as a sort of a Government bank and that feeling, though strictly not justified, did give it command over general public confidence that enabled it to draw enormous deposits and a large clientele. The nationalisation of the Imperial Bank and the amalgamation of some State-associated Banks led to the creation of the State Bank of India. The formation of the State Bank of India was basically the outcome of the recommendation made by the Rural Credit Survey report which had emphasised the urgent need for extension of banking facilities on a large scale, particularly in rural and semi-urban areas of the country. The State Bank, in fact, is a remarkable evidence of the intense feeling in favour of Government-owned organisations as the best media for promoting economic development which has permeated Indian thinking since 1950. The functions of the State Bank have been more or less modelled on the lines of the Imperial Bank of India which it took over. It has, however, the following special features :

(i) The Central Government can issue directions in regard to matters of policy involving public interest ;

(ii) A statutory obligation has been imposed on the bank to open 400 new branches during the five years

1955—1961, though Government may extend the period, if necessary ;

(iii) An "Integration and Development Fund" has been created to meet losses in the case of unremunerative branches. The fund is fed by paying into it the dividends due to the Reserve Bank of India for the share capital it holds of the State Bank of India.

9·2 *Constitution.* As a nationalised institution, it naturally is under considerable control of the Government of India and the Reserve Bank of India. The State Bank of India Act requires that the Reserve Bank of India should always hold not less than 55 per cent of the share capital of the State Bank of India. At present the Reserve Bank of India holds about 92 per cent of the capital, the rest being held by private shareholders. The general management of the Bank is entrusted to a Central Board of Directors, which consists of a Chairman, a Vice-Chairman, not more than two Managing Directors, eight Directors nominated by the Central Government in consultation with the Reserve Bank of India, six Directors elected by the Bank's shareholders other than the Reserve Bank, one Director nominated by the Central Government and one Director nominated by the Reserve Bank of India. The Chairman and Vice-Chairman, except in the case of first appointments, are appointed by the Central Govt. in consultation with the Reserve Bank of India and after consideration of the recommendations, if any, of the Central Board made in that behalf. The Managing Director is appointed by the Central Board with the approval of the Central Government. The Board is enjoined by the Act to function on business principles, regard being paid to public interest. The Central Government in consultation with the Governor of the Reserve Bank of India and the Chairman of the State Bank of India is entitled to issue directives to the Bank on matters of policy involving public interest.

9·3 *Nature of the State Bank of India.* The bank, though a nationalised undertaking, is essentially a commercial banking institution. Though the provisions of the State Bank of India Act are largely imitations of the corresponding provisions of the Imperial Bank of India Act, suitable modifications and adaptations have been made to enable the State Bank of India to play appropriately its assigned role of assisting in the field of rural finance, consistent with sound banking principles. The chief features of the Act are

(i) the State Bank of India can acquire and hold shares in the capital of other banking institutions,

(ii) power to form other banking institutions and conducting them as subsidiaries,

(iii) provision of a summary procedure of voluntary amalgamation of any bank with the State Bank of India

(iv) its appointment as the sole agent of the Reserve Bank at places where the banking department of the Reserve Bank has no branches but where the State Bank has branches.

9·4 *Subsidiary Banks.* The State Bank of India (Subsidiary Banks) Act was passed in September 1959 enabling the State Bank to take over eight State-associated banks as its subsidiaries. The following eight banks are accordingly functioning now as subsidiaries of the State Bank of India: (1) The State Bank of Bikaner, (2) The State Bank of Hyderabad (3) The State Bank of Indore, (4) The State Bank of Jaipur (5) The State Bank of Mysore, (6) The State Bank of Patiala (7) The State Bank of Swarashtra and, (8) The State Bank of Travancore. In respect of all these banks, majority holding has been reserved for the State Bank of India provision having been made for issued capital upto 45 per cent of each of them being held by private persons. Management of these subsidiaries is entrusted to their respective Board of Directors, which include prominent non-officials interested in the development of a region and on which private shareholders of the respective banks have separate and independent representation. These subsidiary banks maintain their own individuality and independence in their day-to-day operations, while the State Bank has general powers of control, supervision and direction. These subsidiaries have at present a total number of 324 branches and 47 other offices and the total deposits of these banks stood at Rs. 104·4 crores as on 24th June, 1960.

9·5 *Capital Structure.* The authorised share capital of the State Bank of India is Rs. 20 crores, while its issued share capital, *i.e.* paid up capital is Rs. 5·63 crores. At the time of nationalisation, the former shareholders of the Imperial Bank were given an option to acquire in surrender shares of the State Bank of India, or to be paid compensation in Central Government securities. The compensation was calculated on the basis of the average stock exchange value of shares over a period of time. Further, since the intention behind nationalisation of the Imperial Bank was to ensure majority holding by Government, it was provided that the Reserve Bank would transfer to the Imperial Bank shareholders and others only upto 45 percent of the total issued

capital of the State Bank of India, the remaining 55 percent being held by the Reserve Bank and the Central Government. The following figures indicate the capital and reserve of the State Bank of India.

(Rs. Lakhs)

Year	Paid-up capital	Reserve	Total
(1)	(2)	(3)	(4)
1955	5,63	6,35	11,98
1956	5,63	6,38	12,01
1957	5,63	6,63	12,26
1958	5,63	7,00	12,63
1959	5,63	7,20	12,83

The activities of the State Bank of India being multifarious and its position in the banking system being of a very special nature, it is necessary to get a clearer picture of its capital structure. The following statement brings out the position for the last two years for which full details are readily available :

Capital Structure.

BALANCE SHEET AS AT 31-12-1959.

Capital and Liabilities			Property and Assets		
As at 31st Dec. 1958 (Rs.)		As at 31st Dec. 1959 (Rs.)	As at 31st Dec. 1958 (Rs.)		As at 31st Dec. 1959 (Rs.)
5,62,50,000	Subscribed and paid-up capital.	5,62,50,000	52,73,57,496	Cash in hand and with the Reserve Bank of India.	60,31,65,944
7,00,00,000	Reserve fund and other reserves	7,20,00,000	2,73,52,995	Balances with other banks in India and abroad . .	4,52,19,136
1,48,50,000	Integration and development fund	1,68,86,841	2,10,66,667	Money at call and short notice	2,46,66,667

9·5, *Banking Operations.* The advances (including bills) made by the State Bank of India are very large and are the largest made by any single scheduled bank in India. They have been steadily rising and reached on 8th July 1960 the record figure of Rs. 215·7 crores which formed approximately 19 percent of the total advances of all scheduled banks. The detailed figures are given below :

(Rs. Lakhs)

Year	Deposits	Cash in hand and at banks	Investments	Loans and advances including bill discounted and purchased.
(1)	(2)	(3)	(4)	(5)
1955	2,19,80	29,38	1,16,98	1,05,81
1956	2,35,47	27,78	1,06,87	1,40,16
1957	3,66,68	39,52	1,83,43	1,73,48
1958	4,78,68	55,47	2,84,56	1,72,06
1959	5,82,11	64,83	3,77,93	1,66,88

It is necessary to point out that the enormous rise in the deposit liabilities of the Bank, which rose by more than 100 percent since its establishment, is not entirely a rosy picture of mobilised savings and actively created deposits in the traditional sense of the term. Actually, a substantial part of the rise was due to the accrual of rupee counterpart funds in respect of import of commodities under P.L. 480 from U.S.A. In fact, due to this particular feature there was a substantial rise upto the first half of 1960, deposit liabilities (total) being Rs. 595·1 crores in August 1960 as against Rs. 550·5 crores in August 1959. In June 1960 a change of procedure was adopted whereby P. L. 480 deposits were transferred from the State Bank of India to Government, and past accumulations of these funds with the State Bank of India were to accrue to Government in monthly instalments of Rs. 12 crores each. This change in procedure would obviously reduce the total deposits with the State Bank of India and would also reduce its investments in Government securities in which it generally held such funds.

9·6. Achievements.

9·6·1 *Foreign Exchange Business* The Bank has been making special efforts to increase its foreign exchange business and has taken some special steps in this respect, *viz*,.

(i) information service and packing credits,

(ii) direct dealings in foreign currencies,

(iii) issue of Rupee travellers cheques, and,

(iv) financing the import of capital goods on a deferred payment basis.

9·6·2 *Remittance Facilities.* It has substantially extended remittance facilities to both scheduled banks and cooperative credit institutions. This has been done under the Reserve Bank of India Remittance Facilities Scheme. The State Bank of India has also been specially assisting, on its own initiative, remittance facilities to cooperative banks in the reverse direction with a view to facilitating movement of funds towards rural areas.

9·6·3 *Development of Warehousing Facilities.* It has assisted in this very important requirement by not only making contributions to the share capital of the Central Warehousing Corporation but also by evolving an appropriate procedure for granting advances against warehouse receipts.

9·6·4 *Aid to Co-operatives.* Responsiveness to financial requirements of cooperative institutions has been a welcome aspect of the State Bank's credit policy. The important measures of assistance adopted by it have been,

(i) granting of special and normal remittance facilities, often at par,

(ii) sanctioning credit limits to co-operative banks against various types of securities,

(iii) lending support to the debentures issued by co-operative central land mortgage banks by subscribing to and granting advances against these debentures,

(iv) providing interim accommodations to land mortgage banks on Government guarantee for financing their loan operations pending floatation of debentures,

(v) paying particular attention to the financing of co-operative marketing and processing societies, without, however, disturbing the basic relationship between co-operative central financing agencies and other co operative societes.

9·6·5 *Provision of Co-ordinated Finance to Small Scale Industries.* The Bank had initiated a pilot scheme for financing small scale industries in a few selected centres in 1956. As the experience gained was extremely satisfactory, the Bank undertook from January 1959 a more comprehensive scheme

for financing small scale industries at all its branches. Financing of small scale industries is now a part of the usual business of the bank. Even though the earlier hesitant attitude of an 'experimental' basis has been abandoned the emphasis is naturally not uniform in all its centres. The State Bank of India has selected a few of its branches as 'intensive' centres where concentrated attention is given to credit requirements of small scale industries.

9·6·6 *Participation in Credit Guarantee Scheme.* The Government of India have recently put into operation a Credit Guarantee scheme. Under this scheme, the Reserve Bank of India acts as a guarantee organisation to enable extension of institutional lending to small scale industries by affording banks etc, a measure of insurance against possible default by borrowers. The guarantee funds are provided by the Government of India from which the quantum of guarantee is made available. The guarantee is on a sliding scale, *i.e.*, smaller loans receiving proportionately greater guarantee coverage than larger ones. The scheme has been put into operation on an experimental basis in 22 districts for a period of two years, from 1st July, 1960, and, 70 offices (including 4 local head offices) of the State Bank of India are covered under this scheme. The working of this scheme is being watched with interest, especially with a view to ascertaining whether such guarantees have any effect in reducing banker's normal caution or increasing evasion of payment by the ultimate borrower.

9·6·7 *Support to Gilt-edged Security Prices.* The Bank has utilised a large part of its deposits in augmenting its portfolio of Government securities. Its holding of such securities increased from Rs. 105·1 crores in 1955 to Rs. 382·5 crores in 1960, and constituted 51·4 percent of the total investments in such securities of all scheduled banks in 1960.

9·6. 8. *Emphasis on Advance to Industry.* As is naturally to be expected, the Bank's policy relating to granting of advances has been in line with the pattern of planned development during the second plan period during which substantial development of industries took place. The statement given on next page illustrates the purpose-wise classification of the advances made by the State Bank of India.

9·7 *Expansion of Banking and the State Bank of India.* An important factor influencing the decision to nationalise the Imperial Bank of India and forming the State Bank of India, was the failure of the former to adequately assist in expanding banking facilities by opening adequate numbers of

Percentage Distribution of Advances

Purpose	Percentage to total advance in 1959	1960
(1)	(2)	(3)
1. Industry	65·4	68·5
2. Commerce	15·8	16·7
3. Agriculture	0·4	0·5
4. Personal and professional	8·6	6·9
5 Others	9·8	7·4
	(100)	(100)

N. B. Figures are approximations based on rough grouping.

branches with in a defined period. With the increasing tempo of economic activity and the growing necessity to take banking to the doors of the humble dwellers in less populated centres, the country was impatient with the slow and "lordly" attitude of the Imperial Bank of India. Thus, the main object of the establishment of the State Bank of India was to extend banking facilities, on a large scale, especially in the rural and semi-urban areas of the country. Accordingly, section 16 (5) of the State Bank of India Act laid down that the Bank has to open 400 branches within a period of five years after 1st July 1955. It is a matter of gratification that on the 1st June 1960, with the opening of 400th new branch at Kairana, U. P., the bank fulfilled this obligation before schedule. It is significant that most of these 400 new branches have been opened at relatively small places where banking facilities were either inadequate or non-existent. Of the 400 centres at which branches were opened by the Bank, all except 24 have a population not exceeding 50,300; 90 have a population between 25,000 and 50,000; 209 between 10,000 and 25,000 and 77 below 10,000. At 64 centres no banking facilities whatsoever existed and at 40 centres no banking facilities were available within a radius of 20 miles. The bank had on 31st August 1960, a total of 894 offices comprising four local head offices, an office in London, five offices in Pakistan, one office each in Burma and Ceylon, 647 branches and 235 sub-offices in India. These 824 offices of the State Bank of India together with the 324 branches and 47 other offices of the eight subsidiary banks form a network of an integrated banking structure of 1265 offices spread over the entire country. Total deposits of the composite structure amounted to R. 699 5 crores out of Rs. 1,966·0 crores of deposits of all scheduled banks at the end of August 1960. This

structure may be regarded as capable of providing banking and remittance facilities within easy reach from all places of importance as also being sufficiently responsive to Government policies adopted for a rapid development of the country's economy.

9·8 *Conclusion.* Even the most ardent advocate of extension of the public sector to economic life is generally hesitant of nationalisation of commercial banking. The experiment in selective nationalisation of banking, which the inauguration of the State Bank of India initiated was, therefore, a bold step. Greater coordination of monetary, economic and financial policies is undoubtedly an urgent necessity in a planned economy, but normally this national responsibility is achieved through the Central Bank of the country. With the growing importance of planning, and the widening field of the public sector (which involved, in many cases, acceptance of the principle of nationalisation of particular industries or particular sectors of economy), the need for a full alignment between State economic policy and banking operations becomes increasingly more urgent. The need was recognised as early as 1956. The experience of the last five years is ample proof, if indeed proof were needed, of the significant contribution that a nationalised commercial bank can make to foster banking activity and for providing a lead (if necessary, by economic compulsion) towards a progressive social policy in banking. The success of the State Bank of India in achieving a blend between commercial outlook of a banker and the progressive outlook of a social planner has indeed been remarkable. Whatever mental reservations one may have held in the past about the possible wisdom of nationalisation of commercial banking are now swept away, and, one can look forward with courage and conviction to the extension of this field. Whether the extension is undertaken immediately or after some time is not very important, for its ultimate adoption is both desirable and inescapable.

10. Indigenous Banking.

10·1 *Definition.* Indigenous banking has always been distinguished from pure money lending, but it has rarely been possible to define the indigenous banker with any degree of precision. This difficulty has been mainly the result of the endless variety of functions performed by him, and, what is more complicating, the variations in functions performed by them as between individual bankers as also by the same banker at different points of time. The Indian Central Banking Enquiry Committee[155] of 1931 while suggesting the advis-

155. Report, para 107.

ability of dealing with the problem of the money-lender separately from that of the indigenous banker defined the latter as meaning

> "............all bankers other than the Imperial Bank of India, the exchange banks, the joint stock banks and the co-operative societies, and that the expression includes any individual or private firm receiving and dealing in *hundis* or lending money."

The above is hardly a definition. It seeks to demarcate between the two in terms of functions, and attempts to suggest that non-performance of certain functions debars the institution from being classified as a banker. Such an approach would not be unreasonable, were it not for the fact that the very concept of the primary function of banking is debatable. In western concepts of banking there has been a tendency to regard operating with borrowed funds as the *sine qua non* of banking. In other words, accepting deposits (operatable through cheques) was the primary function of banking, as all other functions more or less were incidental to the necessity of providing service to the depositor. One would obviously be inclined to accept such a view were it not for the fact that the indigenous banker is part of an indigenous system which could hardly be judged in terms of imported ideology. Banking must create institutions which will fit into the life of the country, get adapted to the practices in the country and be adjusted to the diverse needs of the population. An Indian banker needs to be *sui generis*; he 'must be as Indian as the Ganges'. If so, the indigenous banker is perhaps as much a banker in India as the Lloyds are in England. It is true that the drawing of cheques is not a matter of common practice with some of the indigenous bankers nor is their reliance on deposits as a source of working capital great, yet there is no denying that as urban and rural financiers, they perform functions that range as widely from being depositories of spare funds, issue of drafts, remitting of money to money-lending, pure and simple. It thus seems best to regard the indigenous banker as those that conduct their business along indigenous lines and who have, by tradition and convention, always been regarded as bankers by the people of the country. In such an approach there would obviously be individual cases where it would not be easy to demarcate, but such cases are not many and do not vitiate the convenience of the general approach.

10·2 *Distinction with Money-lenders.* It would be useful to remember that the whole concept of the so called distinction between indigenous bankers and moneylenders

is the outcome of banking theory based on western economic thought. In India, neither the people nor those who style themselves as bankers (indigenous, in the language of modern banking) observe any rigid distinction between banking and moneylending. In fact, even in western countries the distinction was not very clear prior to 1844, and the transition from one to the other, *i.e.* from money-lending to banking has been more of an evolution, both in functions and concepts, than brought about by rigid definitions. The most appropriate way to analyse the distinction is to regard it as a difference of degree rather than one of kind, though in extreme cases wide differences of degree do verge on differences in kind, It is obviously correct that

> "The indigenous banker combines banking and business, but in his case banking is primary. This is largely a difference of degree, and the other differences between.........the indigenous banker and the moneylender are of much the same nature. The indigenous banker finances trade and industry rather than consumption ; the urban money lender consumption rather than trade. Both banker and moneylender advance partly with, and partly without, security but the banker more often with than without, and the moneylender probably more often without than with. The banker is generally particular about the objects for which money is required ; the money lender is less careful."[156]

10·3 Functions and Nature of the Indigenous Banker.

10·3·1. *Functions*. It is generally admitted that the functions of the indigenous banker in the internal economy of the country is a useful one. He finances the agriculturist he assists in the movement of the crops to consuming areas or to the ports. They are depositories of spare funds and issue drafts, while it is not unknown, though it is certainly unusual, for some of them to allow 'cheques' to be drawn upon them. They grant advances against material security often in small sums drawable at the convenience of the customers,—a practice which greatly resembles the overdraft facility extended by organized banks·[157] Their main concern being rural areas, they are primarily financiers of agricultural trade,

156. Vide Report of the Indian Central Banking Enquiry Committee, p. 73.

157. See a remarkably painstaking and detailed survey undertaken by V. Krishnan in his Indigenous Banking in South India. Some of his conclusions are applicable equally to the whole of India.

though they do not keep themselves aloof from general trade and industry. However, by the very nature of their operations, their contacts are with the small trader and the small industrialist. They play an important part in financing trade and industry and in connection with such financing operations he does a good deal of general banking business, such as discounting *hundies*. buying and selling remittances, receiving deposits and advancing loans against stock in trade.

10·3·2. *Nature of Business.* The majority of the indigenous bankers are multipurpose agencies, combining some form of trade with banking. They do not distinguish between the capital employed in banking from that employed in trade. While some of them still consider banking proper as their principal business, majority of them are steadily becoming traders or merchants principally but employing their surplus funds in banking business.

10·3 3. *Methods of Business.* There is a common belief that indigenous bankers are slip shod agencies with little organized activity. Such views are mainly the result of a confusion between them and money-lenders Whatever may be the shady practices adopted by the moneylenders, so far as indigenous bankers are concerned, even the Indian Central Banking Enquiry Committee[158] were forced to the conclusion that

> ".........the indigenous banker's operations are not attended with formalities and delays. His accounts are kept in a simple and economical way but are accurate and efficient. He is easily and always accessible. His establishment is not costly and there is no elaborate staff."

These are important qualities for a country like India where the majority of the people are poor and illiterate and are hardly in a position to afford a costly banking service system.

10·4 *Future of Indigenous bankers.* It is difficult to make any accurate or reliable estimates about the role of these institutions in the economic life of the country as data relating to their activities is neither regularly published nor even probably regularly maintained by the bankers themselves. However, since the indigenous bankers have been carrying on their activities continuosly, they must be having adequate data for their own purposes.* It would be obvious-

158. para 127.
* Dr. Krishnan's study has revealed some very interesting facts.

ly useful to make a special study of their activities and the contribution they make to the economy of the country. In recent times, the indigenous bankers are undoubtedly being gradually squeezed out both by the development of co-operative banking on the one hand and the extension of commercial banking to non-urban areas on the other hand. Yet, they have continued and persisted with a tenacity that speaks well of their utility (in the economic sense without its moral association) to the economy. Thus, judged by the traditional norms of stability, adaptability and initiative, the indigenous bankers must be regarded as coming out with flying colours for they possess these three qualities in a remarkable degree.[159] It would be idle to pretend that these indigenous bankers are without defects ; it would, however, be equally unjust to hold that they have no contribution to make in the future development of the country. However, the dilemma really originates from the reluctance of the indigenous bankers to institutionalise themselves in an era of progress through institutional banking, which is a primary requirement for co-ordinated and controlled development of credit. Inspite of a declining volume of business, the indigenous banker still continues to play a significant role in the finance of internal trade, especially if account is taken of the finance extended by them to enable a rise in the retention-ratios of the Indian agriculturists. Even as late as 1954, we find the Shroff Committee[160] on Finance for the Private Sector observing as follows :

> ".........no detailed statistics are available regarding the operations of these agencies for the country as a whole...........Nevertheless, the importance of indigenous bankers and money-lenders in the financial structure of the country is too well known to need further emphasis ; for instance, it is estimated that indigenons bankers finance about 75 to 90% of the total internal trade of the country."

It is difficult to assess the accuracy of the figure given by the Shroff Committee, but even if a fairly wide margin of error were permitted the significance of the indigenous bankers would still remain fairly considerable. In fact, the

159. For instance, G. Findlay-Shirras, an author none too charitably disposed tawards Indian organizations, admits, even though perhaps reluctantly, that for the indigenous banker "to dishonour a hundi is an event of rare occurrence." See, Indian Finance and Banking, p. 341.

160. Report p. 66 ; it is a pity that the N.S.S. has not been used for collecting data on such a useful aspect instead of wasting energies on repeatitive consumer expenditure data collection.

Shroff Committee were sufficiently impressed with the possibilities of these bankers to recommend that indigenous bankers should try to organise their banking business and steps should be taken to encourage the rediscounting of their Usance Bills by the Reserve Bank of India through scheduled banks.

10·5 *Thg Indigenous Banker and the Reserve Bank of India.* Even before the Reserve Bank was established, the Indian Central Banking Enquiry Committee felt that when the Reserve Bank is established the indigenous banker should be brought into direct relations with the Reserve Bank and thereby provided with rediscount facilities from that institution. This recommendation was made because it was thought to be "of the greatest importance that in the interests of both the general public and the indigenous bankers themselves, steps should be devised to strengthen the position of these bankers." It shold, however, be borne in mind that the Indian Central Banking Enquiry Committee held very conservative ideas about banking and were of the view that only such indigenous bankers as were engaged in banking proper, or were prepared to shed their business other than banking should be entitled to the privilege of rediscounting facilities as "the Reserve Bank can only rediscount bank-endorsed paper."

The proposals of the Reserve Bank of India, made in 1937, contemplated the indirect linking of indigenous bankers through the scheduled banks. This was subsequently abondoned and a revised proposal on the lines recommended by the Indian Central Banking Enquiry Committee put forward. The committee's proposals were broadly as follows :—

(a) abandonment of non- banking business by the indigenous bankers,

(b) non-insistence on maintenance of detailed statistics and submission of frequent statistical returns by these bankers,

(c) a lower standard of owned capital for their eligibility,

(d) maintenance of proper books of accounts by the indigenous bankers with regular audit by qualified auditors, and,

(e) exemption of the smaller indigenous bankers from the rule of maintaining compulsory deposits and reserves with the Reserve Bank.

In spite of the considerably greater liberality of the revised scheme, little headway could be made because of the reluctance of the indigenous bankers to abandon their non-

banking business. The indigenous bankers remained outside the purview of the Reserve Bank's influence, though, even while isolated, the intrinsic worth of their business remained high. Later, the Reserve Bank agreed not to insist on immediate abandonment of non-banking business by these bankers and required only separation of such business from the banking business, with a stipulation to discard it within a specified period. Even this does not seem to attract the indigenous bankers, so that the inescapable conclusion seems to be that they have little to profit by their integration with the general banking system and much to lose. This would, however, be the position as long as the profitability of the particular type of business carried on by them is high ; and, it will remain high as long as, due only to the unfortunate discount put on traditional Indian type of business, there are first class securities which are treated as second class credit by organized banking, leading to such securities forming the backbone of the business of indigenous bankers. Things, however, are rapidly changing. The Reserve Bank of India's bill market scheme has proved to be a success and will steadily grow in significance. The growth of warehousing facilities under the leadership of the Central Warehousing Corporation, and assisted by State Warehousing Corporations, is bound to lead, in course of time, to the increasing use of licensed warehouse receipts as the basis of bank advances. There is also the development of the integrated system of rural credit and State assistance to co-operative credit, both of which will cause a decline in the agriculturist's dependance on the indigenous bankers. All this means a rather bleak future for the indigenous banking system, and, if they were wise with sufficient foresight, they would do well to read the writing on the wall and submit, in their own interest, to the supervision and control of the Reserve Bank of India by formalizing their own methods of business and crossing the "Rubicon" so as to become bankers in the modern sense of the term and cease to be the sort of multipurpose functionaries that they now are.

11. The Reserve Bank of India.

11·1 *Nature and Evolution.* Traditional economic theory prided in a distrust of Government in the field of Central banking and currency management and believed that a Government was "not as sensitive as a bank to the conditions in the financial and commercial world."[161] It is doubtful whether lack of knowledge and adaptability in a Govern-

161. Kisch and Elkin—Central Banks, p. 73.

mental organisation could be regarded even now as being as unsatisfactory as it was a quarter of a century ago for with the increasing role played by Government in economic matters both the competence and the suitability of its organisations to deal with banking, commerce and industry appropriately has increased. Even then, there are great advantages in leaving executive and day-to-day work relating to money and banking in the hands of a specialised institution and confining the role of the Government to considerations of policy and overall guidance. Thus the modern trend has been continuously towards having nationalised institutions as Central Banks with close co-ordination and intimate contact between it and Government. The old controversy as to the rival merits of a shareholder's bank versus a state ownership principle, whatever its theoretical significance, has no practical importance for India to day. The Reserve Bank of India began as a shareholder's bank and ended up in 1949 by being a State-owned and State-controlled bank after a brief, but unsuccessful, attempt in 1940 to combat the evil of concentration of shares in particular areas of the country with large holdings for a few individuals.

11·2 *Constitution.* The Hilton-Young Commission intended the central banking institution to overcome "the inherent weakness of a system in which the control of currency and credit is in the hands of two distinct authorities whose policies may be widely divergent, and in which the currency and banking reserves are controlled and managed separately one from the other." This, together with the supreme necessity of maintaining India's financial stability and credit, both at home and abroad, to ensure the success of the Constitutional Reforms of 1935 led to the establishment of the Reserve Bank of India. In fact, it was a reluctant 'gift' grudgingly surrendered as would be apparent to anyone who has studied the history of the Reserve Bank legislation before the Indian Legislative Assembly, for we find that as soon as the wishes of the Assembly were found to be different from that of the Government, the Finance Member (Sir Basil Blackett) simply announced the decision of Government that they had no intention of proceeding with the Reserve Bank of India Bill. The Reserve Bank was established under the Reserve Bank of India Act, 1934 and commenced operations on April 1, 1935. Initially a shareholders' establishment, the Bank was nationalised with effect from January 1, 1949. The general superintendence and direction of Bank's affairs is vested in the Central Board of Directors consisting of 15 members, namely the Governor, three-deputy-Governors and eleven other directors nominated by the Central Government under

various sub-sections of Section 8 of the Reserve Bank of India Act, 1934. According to the preamble to the Reserve Bank of India Act, 1934, the main function of the Reserve Bank is "to regulate the issue of Bank notes and the keeping of reserves with a view to securing monetary stability in India and generally to operate the currency and credit system of the country to its advantage". The Bank is given the sole right of note issue in India. Also, wide powers both under the Reserve Bank of India Act, 1934 and the Banking Companies Act, 1949 are vested in the Reserve Bank to enable the Bank to control, inspect and develop commercial banking system. The Bank acts as banker to the Central and State Governments, the commercial banks and some other financial institutions. It advises Government on economic matters in general and on financial problems in particular. The Bank maintains the exchange value of the rupee through purchase and sale of sterling from/to banks at specified rates and is the custodian of the country's international reserves. It exercises control over payments and receipts for international transactions in conformity with Government policy. With the increased emphasis placed on development planning, the range of functions of the Reserve Bank has become wide and varied. The Bank's responsibilities now comprise development of an adequate and sound banking system for catering not only to the needs of trade and commerce but also of agriculture and industry and it has assisted in the development of institutional arrangements for expansion of credit to these sectors. The conversion of the Reserve Bank into a full-fledged State-owned central bank was undertaken with the object of attaining "greater coordination of the monetary, economic and financial policies" of the country. At present the Government of India are specifically authorised to issue directions to the Reserve Bank from time to time as it deems necessary in the national interest and such directions are issued after joint consultation between the Finance Minister and the Governor of the Bank. It is clear that with the growth of centralised planning, the conservative idea of an 'independent' central bank is a misnomer, for in a planned economy central banking is only one among a number of tools in the hands of Government to secure rising standards of living, higher levels of employment and balanced development. There is nothing inherently wrong in having a nationalised institution as a Central Bank in an era of expanded volume of State enterprises, for as has been aptly stated[162] "......if State ownership is a tradition soundly established by the country, a

162. Kisch and Elkin—Central Banks, p. 25.

State Bank should in theory be as capable of carrying out a national policy as an institution of an independent or quasi-independent character." In India, whatever else may or may not have been established as a tradition, the tradition of State-ownership has been fully established, and in the present context it is idle to believe that the Central Bank of the country could achieve any nationally beneficial results without the support and authority of the Government being available to its policies. The wisdom of having a State-owned Central Bank for India was outlined, strangely enough, in 1913 by J.M. Keynes[163] as follows :—

> "A Central Bank must necessarily stand in a somewhat close relation to Government. If the Bank is to be useful, it must have the management of the Government balances and the note issue. It would be contrary to experience elsewhere and to what seems reasonable for India to hand over these functions to a purely private institution. If Government is to interfere at all, it cannot help involving itself in ultimate responsibility for the Bank, and if it is thus to involve itself, its powers must be sufficient to permit an effective supervision. From a Government with feeble powers and placed in the position of interested but irresponsible critics, there would be a greater likelihood of vexatious interference; while too great a dependence on the terms of the Bank's charter must tend to make these terms rigid and narrow for practice".

These observations are as true to-day as when they were made, and it is an irony of fate that it was only after nearly 25 years of its establishment was it possible to make the Reserve Bank of India what the representatives of the people of the country had wanted as early as 1927.

11·3 *Functions.* The necessity for a central banking institution in India for securing the development of the Indian banking and credit system on a sound and proper basis has been emphasised by various authorities from time to time. The traditional functions of a Central Bank are well-known, and, apparently the Reserve Bank of India must have these functions if it is to acquire the status of a Central Bank or achieve the ends for which it has been established. It is, however, important to bear in mind that the true success of a central banking institution does not lie in its list of functions but in designing it in such a way as to meet the practi-

163. Annexe to the Report of the Chamberlain Commission (1913).

cal requirements of the country and making it adaptable to the banking organization of the country which it is intended to serve. Thus, it seems rather puerile to assess the functions of the Reserve Bank of India by comparing it with those of Central Banks in other countries as the economic situation in India is not obviously a replica of what exists elsewhere. We may broadly classify the functions of the Reserve Bank of Ind'a as follows :—

I. Basic Functions.

(i) Issuing of paper currency,

(ii) Acting as banker to Government,

(iii) Performing the role of banker to other banks, and holding compulsory reserves,

(iv) Controlling credit expansion and contraction,

(v) Ultimate provider of rediscounting facilities and lender of last resort ;

II. Supplementary Functions.

(vi) Maintenance of Foreign Exchange value of the Rupee,

(vii) Provision of adequate credit to trade, commerce, industry and agriculture,

(viii) Operating measures of exchange control and banking supervision as envisaged under relevant laws ;

III. Promotional Functions.

(ix) Ensuring expansion and spread of banking, and improving banks through inspections,

(x) Promoting the development of a bill market for the country,

(xi) Assisting in Plan-objectives in the field of banking, *e.g.*, provision of agricultural credit through cooperative banking ;

IV. Incidental Functions.

(xii) Collection and publication of monetary and financial statistics,

(xiii) Dissemination of banking wisdom,

(xiv) Acquinting member-banks with developments and implications of State policy in monetary matters,

(xv) Advising on methods of voluntary internal cooperation amongst the member-banks,

The classification and the enumeration undertaken above is essentially for convenience of understanding and listing, rather than for providing a logical grouping. It is clear that some of the functions are interdependent and aid each other. For example, the more effectively the Reserve Bank is able to disseminate banking wisdom the easier would it be for it to enforce a given credit control policy ; or, again, it is only by ensuring adequate expansion and development of banking that it could ensure appropriate provision of credit to all sectors and all regions.

11·4 *Banking Operations.* These operations of the Reserve Bank can be grouped under three broad heads *viz.*:

(a) day-to-day management of government finances and foreign exchange reserves,

(b) development and strengthening of the institutional set-up for credit supply,

(c) regulation of money and credit in the economy.

The undertaking of Government business and the management of Government transactions involve large day to day transfers of money from place to place, and as between the treasury and the community. The Government keeps some of its funds with the Reserve Bank free of interest. The Reserve Bank has to discharge the important function of making ways and means advances to the Central and State Governments repayable within 90 days, to purchase and sell Government securities, manage the public debt, to receive money on behalf of Government and make payments as per order. The transacting of banking business of the Government of India is a right and an obligation of the Reserve Bank under the Act which enjoins the Bank to accept money on account of the Central Government, to make payments on its behalf and also to carry out its exchange, remittance and other banking operations including management of public debt. So far as the State Governments are concerned, the Bank performs similar functions on their behalf through agreements entered into with them. For administering exchange control and acting as the custodian of the country's exchange reserves, the Reserve Bank acts as agent of the Central Government.

So far as extension of credit facilities are concerned, the Reserve Bank's activities could be demarcated between

(a) those relating to agricultural credit, and

(b) those relating to the channelling of funds to industry.

11·4·1. *Agricultural Credit.* In the field of Agricultural credit*, its activities are :

(i) aiding State Governments to formulate schemes for reorganisation of the co-operative movement,

(ii) financial assistance to farmers through agencies of State and Central co-operative banks, and, Central land mortgage banks,

(iii) granting financial assistance to State Governments to enable them to contribute to the share capital of co-operative societies,

(iv) conducting training courses for co-operative personnel, and

(v) inspection of co-operative banks on a voluntary basis designed to improve the machinery and operations of co-operative credit.

The importance of the role of the Reserve Bank in regard to Agricultural credit was recognised from the very outset and the agricultural Credit Department of the Bank was started simultaneously with the Issue and Banking Departments of the Bank in April, 1935. The Reserve Bank Act provides for assistance to agriculture. The Act enjoins that the Bank cannot make advances to agriculturists direct and can extend accommodation only through scheduled banks or co-operative banks. Initially the Bank's advances in this field were restricted to short term advances mainly for tiding over a temporary or seasonal shortage of funds. This restriction, however, has been subsequently removed by statutory amendments and at present the Reserve Bank's assistance to Co-operative Credit covers :—

(1) For seasonal agricultural operations and marketing of crops, under Section 17 (4) a, 2 (b) or 4 (c) of the Reserve Bank Act,

(2) Medium-term loans to State Co-operative Banks for agricultural purposes, under Section 17 (4AA) of the Act,

(3) Through National Agricultural Credit (long-term operations) Fund, covering

(a) medium-term loans to State Co-operative Banks for agricultural purposes under Section 17 (4AA) read with 46 A (2) (b),

(b) long-term loans to State Governments for contribution to the share capital of Co-operative

* See, Chapter IV,

Credit Societies under Section 17 (4 AA) read with 46 A (2) (a),

(c) long-term loans to Central Land Mortgage Banks under Section 17 (4 AA) read with 46 A (2) (c) of the Act, and

(d) rural debentures under Section 17 (4 AA) read with 46 A (2) (d) of the Reserve Bank of India Act.

The accommodation made available under these categories to the State Co-operative Banks is indicated in the table given below :

(In lakhs of rupees)

Year	Section 17 (2)(b) Advances	Section 17 (2)(b) outstanding	Section 17 (4)(a) Advances	Section 17 (4)(a) outstanding	Section 17 (4)(c) Advances	Section 17 (4)(c) outstanding	Section 17 (4)(A) Advances	Section 17 (4)(A) outstanding	Total Advances	Total outstanding
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
1951-52.	1.99	1,96	4,89	2,26	4,41	3,60	—	—	11,29	7,81
1955-56.	44	39	10,36	2,14	12,59	9,94	41	51	23,80	12,98
1958-59.	—	—	15,90	3,47	56,70	41,02	2,68	4,95	75,28	49,44
1960-61.	—	—	26,97	3,93	115,41	77,84	4,29	7,63	146,66	89,40
1961-62.	—	—	32,33	4,90	153,39	106,99	7,21	10,92	192,92	122,80

Source : R. B. I.

N. B. Columns (8) & (9) cover Section 17 (4AA) from 30th April 1960.

A clearer idea of the relative growth of advances under the different categories can be got from the following reclassified figures on page 393.

11·4·2 *Industrial Finance.** The Reserve Bank has in recent years been devoting considerable attention to channelling of funds to industry. Through its Bill Market Scheme the bank not only supplements the resources of commercial banks in the busy season but uses it as an instrument for according preferential treatment to industry. The Bank has participated in the

* See Ch. VI.

Co-operative Credit

(In Lakhs of Rupees)

Year	For (1)		For (2)		For 3 (a)		For 3 (b)		For 3 (c)		For 3 (d)	
	Amount drawn	out-standings	Amount drawn	out-standings	Amount drawn	out-standings	Amount drawn	out-standings	Amount drawn	out-standings	Amount drawn	out-standings
1951-52	537·30	339·20	...	...	...	...	...	...	...	...	...	...
1955-56	2299·78	1233·48	30·75	40·52	10·59	10.59	...	...	...	...		
1958-59	6755·55	4256·32	...	...	268·44	494·84	574·48	1318·33	...	...	26·88	26·28
1960-61	13166·16	7914·42	...	...	467·90	763·19	274·58	1995·17	...	...	33·17	107·15

Source : R. B. I.

share capital of the Industrial Finance Corporation and State Financial Corporations and is represented on their Boards of Directors. The Bank extends short-term credit to the Finance Corporations. Under the Reserve Bank of India (Amendment) Act, 1960 the Bank is empowered to grant them medium-term loans. The Bank also inspects State Financial Corporations with consent of the Central Government. Another important landmark was the establishment of Refinance Corporation for Industry in 1958 with a view to providing re-finance for medium term loans granted by member banks to medium-sized units in the private sector. Also the Reserve Bank, as agent of the Government of India, has been implementing from July 1960 a scheme (on an experimental basis) for the guarantee of loans given by approved institutions to small-scale industries. The scheme which covers 22 districts provides for sharing of any losses in respect of these loans between the Government and approved lending institutions.

The finance provided is as follows :—

Industrial Finance

(Thousands of Rupees)

Year (End of year figures)	Long term Finance to Industrial Finance Corporation		State Finance Corporations		Medium term Finance to I.F.C. under section 17 (4B) (b)
	Shares	Bonds	Shares	Bonds	
(1)	(2)	(3)	(4)	(5)	(6)
1951-52	102,70	—	—	—	
1955-56	102,70	200,00	170,00	—	106,50
1958-59	102,70	200,00	200,00	—	93,75
1960-61	102,70	200,00	235,00	—	51,00

Source : R. B. I.

N. B. For colum 6, figures against 1955-56 relate to 1956-57. These figures are outstandings as on last Friday.

11·4·3 *Credit Regulation** In the field of credit regulation, the methods used by the Bank are (1) quantitative or general credit control, (2) qualitative or selective credit controls and (3) moral suasion. Under general credit controls are grouped the Bank rate (*i. e.* the rate at which the Reserve

* See Ch. IX.

Bank in practice grants accommodation to banks), open market operations (purchases and sales of Government and approved securities but mostly of Government securities) and variable reserve requirements (*i. e.*, varying the percentage of demand and time liabilities to be kept by banks as reserve with the Reserve Bank). In India, the Bank rate changes have not been frequent. The persent Bank rate is 4 per cent. Open maket operations, are, on the other hand, continuously employed to achieve the dual objectives of regulating yield pattern of Government securities and increasing or decreasing cash reserve of banks, with the intention of bringing about credit expansion or contraction. The power to vary reserve ratios between prescribed limits was vested in the Bank only in 1956. Under the RBI Amendment Act of 1956, the Bank can vary the required reserves of scheduled banks between 5 and 20 per cent for demand liabilities and 2 and 8 per cent for time liabilities. Under the above ceiling limits, the Bank can also direct scheduled banks to maintain with the Reserve Bank additional deposits computed with reference to the excess of bank's demand and time liabilities over the level on a base date notified for the purpose. The latter power was invoked for the first time on March 11, 1960. The notification was superseded by subsequent notification of May 5, 1960 under which scheduled banks have to keep with the Reserve Bank in the form of additional deposits 50 per cent of the increase in their demand and time liabilities after May 6, 1960.

Apart from the above general restrictive credit control measures, the bank has also been operating selective credit controls since May 1956. These controls are being operated with flexibility in the light of changing conditions of supply and demand and with a view to curb speculative tendencies without curtailing supplies for essential purposes. The credit control policy of the Reserve Bank has been analysed in the previous chapter where an attempt has been made to assess the success or otherwise of these policies.

11·4·4. *Banking Extension.* It has been pointed out earlier (vide para 2·2·3) that a vast country like India requires development of branch banking for proper extension of banking services throughout the country.

The bank plays a vital role in strengthening of the commercial banking system and its extension into undeveloped areas. It enjoys fairly extensive powers under the Banking Companies Act, 1949 to license and inspect commercial banks. Branch expansion of commercial banks is regulated by the Reserve Bank in order to prevent excessive expansion in the more developed areas and to encourage their spread

into rural and semi-urban centres. The Bank also attempts to improve the quality of the bank staff through conducting training courses at the Banker's Training College established by it.

11·5 *Reserve Bank as Currency Authority.* The sole right of note issue is a primary function of a Central Bank, and the Reserve Bank of India has been entrusted with this right. It is generally recognised that the issue of paper currency should not be left completely unregulated and the law, therefore, requires maintenance of prescribed reserves against the note-issue.* The function of such reserve initially was the ensuring of convertibilty internally of the paper currency. With the growth of inconvertible currencies, the basic function of the reserve against note-issue has altered and it is now hardly relevant from the point of view of guaranteeing safety. Present day thinking is more inclined towards the requirement of elasticity as the primary consideration in a good note issue system, subject, of course, to prevention of over-issue or stringency, so as to serve the best interest of the currency. For the issue of notes the Reserve Bank maintains a separate department called the Issue Department, the assets of which are kept distinct from those of its Banking Department. The Bank started issuing its own notes at the beginning of 1938, and at present, apart from the one rupee note which are issued by the Government of India,all other notes are issued by the Reserve Bank of India. The separation of the Issue Department and the Banking Department is on the pattern of the Bank of England and is a relic of the now abandoned idea of the Currency School that bank notes alone being money a distinction of principle must be drawn between note-issue management and banking business. The distinction, however, has no significance and, apart from complicating accounting procedure, it serves little useful purpose. The original provision of the Act laid down that of the total assets not less than 40 per cent must under the law consist of gold coin, gold bullion or sterling securities, provided that the amount of gold coin and gold bullion was not at anytime less than Rs. 40 crores in value. With the previous sanction of the Central Government, the Bank could hold gold coin, gold bullion or sterling securities of less than 40 percent of the assets for limited periods on payment of a specified tax on the deficiency. The remaining 60 percent could be held in the shape of rupee securities, rupee coins and prescribed bills of exchange, etc., provided the rupee securities of the Government of India did not exceed Rs. 50 crores, or 25 percent of the total,

* See Ch. IX.

whichever was greater. These provisions were found to be unsuitable after 1950 when India entered into a phase of planned development leading to an expansionist economy requiring financing of the Plan. A change from the so called 'proportional' system of reserve to a fixed minimum reserve was introduced by the Reserve Bank of India (Amendment) Act, 1956 which provided for a minimum holding of foreign securities of Rs. 400 crores, which in an emergency could be reduced to Rs. 300 crores with Government's prior approval. According to the same amendment gold coin and bullion had to be of Rs. 115 crores, with gold valued at Rs. 62·50 *per tola* according to the parity rate agreed to by the International Monetary Fund. On October 31, 1957, this was further amended by an Ordinance, which was later replaced by a Second Amendment Act. Under tbe revised arrangement, aggregate value of gold coin, gold bullion and foreign securities held in the Issue Department should not at any time be less than Rs. 200 Crores, of which the value of gold coin and gold bullion was to be not less than Rs. 115 crores. The amendment further deleted the stipulation of the minimum value limit of foreign securities. These amendments were obviously intended to enable an easier expansion of note-issue. It is indeed a remarkable evidence of public confidence (or, alternatively, of public ignorance) that such drastic reductions have led to no serious outward adverse signs. Some idea of the expansion of note-issue may be got from the table given below :

Issue Department

(In lakhs of Rupees)

Year	A Liabilities: Notes in circulation	A Liabilities: Notes held in Banking Deptt.	Total A or B	B Assets: Gold coin and Bullion	B Assets: Foreign Securities	B Assets: Rupee coin	B Assets: Govt. of India Rupee Securities
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
1951-52	1,141,11	35,82	1,176,93	40,02	603,15	69,13	464,64
1955-56	1,466,64	11,77	1,478,41	40,02	656,42	103,16	678,82
1958-59	1,701,53	15,60	1,717,22	117,76	178,01	130,09	1,291,26
1960-61	1,984,74	7,84	1,992,59	117,76	123,01	119,62	1,632,20
1961-62	2,070,30	25,37	2,095,67	117,76	113,86	116,91	1,747,14

Source : R. B. I.

N. B. 1. Figures relate to last Friday.
2. Gold valued at Rs. 21·24 per tola upto October 5, 1956, and at Rs. 62·50 per tola thereafter
2. Column (7) includes one rupee notes

The enormous expansion of the note issue, which has practically doubled itself in a decade, is apparent from the above table. It is also equally apparent that but for drastic reductions in the reserve requirements and the revaluation of gold, such an expansion could not have been possible.

11·6 *Banking Department and its Functions.* The work of the Banking Department is the medium through which the Reserve Bank functions as Banker to member-banks, lender of last resort and the regulator of credit policy. In view of the declining influence of currency and the growing importance of bank-money, the activities of the Banking Department are in reality more significant. We have examined earlier* the functioning of the credit control policy of the Reserve Bank.

The continuance of a separate Banking Department does not appear to be serving any beneficial purpose. Modern monetary and banking theory recognises that the alleged distinction between paper-currency and bank-money does not, in effect, exist as all forms of money are easily interchangeable. The only practical service that such a demarcation between the two departments could achieve was, to quote the MacMillan Committee on Finance and Industry to provide "a convenient formula for dividing the profits of the Bank............between the treasury and the Bank itself." It was on this particular argument of convenience that the MacMillan Committee were prone to allow the continuance of a long-standing practice, though they were fully conscious that the elaboration of the organisation for this particular purpose was neither necessary nor conducive to accurate results. But even if it were, the argument could not be extended to support the separation for the Reserve Bank of India as the statute now stands with the Bank a nationalised institution. Even prior to nationalisation there was little justification, for the Bank's profits have always been allocated on a specified basis. Upto 15th August, 1947, the arrangement of separate Issue and Banking Departments was probably a means to show courtesy to the elder brother ; upto 1st January 1949, it was perhaps the result of continued inertia ; thereafter, one can only regard the arrangement as one of those 'features' which commonsense cannot explain, if indeed there is any reasonable justification at all.[164] In fact, the present arrangement simply confuses those who understand, while it has no meaning for those who do not understand, and, unless continued clouding of issues were to be regarded as serving a purpose, the sooner the separation is done away with the better it is.

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* See Ch. IX.
164. See Muranjan, S. K. Modern Banking in India pp. 258-261.

The table given below indicates the liabilities of the Reserve Bank of India in so far as they relate to the Banking Department:

Banking Department
(Liabilities)

(In Lakhs of rupees)

Year (Last Friday)	Deposits Central Govt.	Other Govts.	Banks	Others	Other Liabilities	Total of Deposits
(1)	(2)	(3)	(4)	(5)	(6)	(7)
1951-52	180,16	25,06	46,99	65,90	35,90	318,11
1955-56	67,34	62,03	53,24	16,68	59,46	199,30
1958-59	53,83	26,72	67,57	119,07	190,67	267,19
1960-61	76,46	28,99	70,85	87,96	221,39	264,25
1961-62	71,30	15,89	72,73	152,36	231,84	312,27

Source: R.B.I.

The tremendous decline in Government deposits, both Central and States, is the most outstanding feature of the trend revealed by the above statement. Deposits from banks show a natural trend towards increase as one would normally expect from expansion of banking and bank-money. The fluctuating character of deposits from "others" indicates the necessity of having further details about it. Finally, the rapidly rising figure of "other liabilities" needs to be clarified. These "other liabilities" include *inter-alia*, the following:—

(i) paid-up capital of Rs. 5 crores;

(ii) reserve fund of

- (a) Rs. 5 crores upto June 28, 1957,
- (b) Rs. 80 crores from July 5, 1957;

(iii) National Agricultural Credit (Long-term Operations) Fund of

- (a) Rs. 15 crores from July 6, 1956,
- (b) Rs. 20 crores from July 5, 1957,
- (c) Rs. 25 crores from July 4, 1958,
- (d) Rs. 30 crores from July 3, 1959,
- (e) Rs. 40 crores from July 1, 1960, and,
- (f) Rs. 50 crores from June 30, 1961;

(iv) National Agricultural Credit (Stabilisation) Fund of;

(a) Rs. 1 crore from July 6, 1956,
(b) Rs. 2 crores from July 5, 1957,
(c) Rs. 3 crores from July 4, 1958,
(d) Rs. 4 crores from July 3, 1959,
(e) Rs. 5 crores from July 1, 1960, and
(f) Rs. 6 crores from June 30, 1961.

The expansion of activities of the Reserve Bank must mean an increase in total liabilities *i.e.*, total deposits + other liabilities, or col. 6 + col. 7 of the statement given earlier. Further, these total liabilities must be equal to total assets, for in a balance-sheet liabilities = assets. The figures of total liabilities (or assets) for the corresponding years are as follows :—

(In lakhs of Rupees)

Year	Total Liabilities or Total assets
(1)	(2)
1951-52	354,01
1955-56	258,77
1958-59	457,86
1960-61	485,64
1961-62	544,12

It would be interesting to see how the total assets were distributed, for the asset-allocation policy of the Reserve Bank of India is a matter of vital concern to the economy of the country. The table given below gives the details :

Allocation of Assets

(In Rs. Lakhs)

Year (Last Friday)	Notes and Coins	Balances held abroad	Advances and Loans to Govts.	Other Loens and advances	Bills purchased and discounted	Investments	Other assets
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
1950-51	35,98	119,92	94	61,37	3,72	102,09	29,99
1955-56	11,92	89,72	—	79,94	12,23	47,19	17,77
1958-59	15,67	35,05	24,77	113,44	5,18	251,70	12,05
1960-61	7,94	13,24	39,02	185,50	39,17	180,95	19,82
1961-62	25,42	15,84	80,89	177,69	46,60	163,43	34,24

Source : R.B.I.

The assets of the Banking Department reflect the present conditions of the money market. Thus, a low figure under 'Bills purchased and discounted' is an indication of the low rediscounting facilities obtained or made available. It will be seen that this figure was practically insignificant in 1951-52, and has shown a steady growth in recent years, bringing out the growing significance of the bill market and the increasing reliance placed on rediscounting facilities by the banking system. Secondly, the steady rise in the 'Loans and Advances' to Governments, which include from the middle of 1957 temporary overdrafts to State Governments, is a feature that can hardly be regarded as good financial policy, for generally one would expect a special effort on the part of Governments not to be indebted to the Bank at the end of the year. However, in principle, it must be conceded that a better indicator in this respect is the continuous average indebtedness of Governments, which, if the figures of average of Fridays during the year are any guide, were lower in 1960-61 and 1961-62. Finally, the two most important items on the assets side are (a) other loans and advances, and, (b) investments. These two roughly indicate the funds made available to the banking sector and, since the major portion of the investments is in Government securities, the Government sector. Of course, a part of the investments being in the form of shares of Industrial Finance Corporation and State Finance Corporations, they are available indirectly to the private sector.

11·7 *Profits of the Reserve Bank of India.* 11·7·1 *The Concept.* The Reserve Bank obviously could not, and does not, aim at making profits for it functions more to serve the economy than to benefit from the economy. However, its financial operations must involve a profit and loss account, and, since it is a nationalised institution, the profits that it makes (without trying to make them deliberately) is an income to the Central Government for the surplus is payable to the Government of India. Since the profits made, or, more innocuously, the surplus available, is incidental to its working and does not determine its activities, the existence of "profits" for the Reserve Bank is the one case where the concept could be regarded as unobjectionable, even ideologically, in an economy aimed at achieving a socialistic pattern.

11·7·2 *The Facts.*

Profit and Loss Account

	For the year ended June 30, 1960	For the year ended June 30, 1959
INCOME	(Rs.)	(Rs.)
Interest, Discount, Exchange, Commission etc.	47,56,98,191·33	47,25,60,478·53
EXPENDITURE		
Establishment	3,99,90,211·06	3,78,09,386·14
Director's & Local Board Member's fees and expenses	79,157·30	70,519·60
Auditor's fees	22,500·00	22,500·00
Rent, taxes, insurance, lighting, etc.	21,46,682·16	19,29,808·41
Law charges	47,296·40	1,09,229·73
Postage and telegraph charges	3,44,744·30	3,24,117·25
Remittance of treasure	20,27,926·67	46,24,122·47
Stationery etc.	9,61,034·03	8,12,072·10
Security printing (cheque, note forms, etc.)	1,19,78,666·19	114,98,408·34
Agency charges	1,01,12,875·95	1,00,28,088·37
Depreciation and repairs to bank property	46,33,013·68	23,63,393·19
Contributions to staff and superannuation funds	7,32,00·00	4,63,000·00
Miscellaneous expenses	26,09,481·10	24,83,111·06
Net available balance	40,00,12,602·49	40,00,22,721·87
Total	47,56,98,191·33	47,25,60,478·53

Reserve Fund Account

On 30 June, 1959 (Rs.)		On 30th June 1960 (Rs.)
80,00,00,000·00	By Balance	80,00,00,000·00
Nil	By transfer from Profit and Loss Account	Nil
80,00,00,000 00	Total	80,00,00,000·00

The surplus payable to the Central Government during the two years was a little over Rs. 40 crores each.

12. Bill Market.

12·1 *Necessity.* Until recently, the Indian money market had a serious deficiency in the absence of a properly organised bill market which is generally considered to be a vital necessity. The traditional *hundi* possesses features which are not dissimilar to a modern bill of exchange*, but it could hardly be regarded as providing more than a foundation for the development of a bill market on modern lines. The advantages of a bill market are many, *viz.*,

(1) it facilitates the movement of commodities by reducing the locking up of resources as the seller receives payment in advance of payment by the buyer,

(2) it provides short-term funds, especially to agriculturists,

(3) it opens up a suitable opportunity for holding assets in short-term investments by the banks,

(4) it is a perfect security as it carries with it the guarantee of both a bank and the individual so that it is both ready money and cheap money,

(5) it is self-liquidating and, hence, self-retiring.

12·2 *Essentials for Development of a Bill Market.* It is obvious that a bill market cannot be brought into existence unless certain conditions are satisfied. It is necessary to have legal recognition to such documents and use of such facilities for investment of funds by the banking system. The existence of specialized houses for 'acceptance' of such bills is a convenience but not an inescapable necessity. The era prior to the establishment of the Reserve Bank of India was unfavourable to the growth of a bill market mainly because of the Imperial Bank's uncompromisingly hostile attitude to Indian *hundis*, and, its being both a competitor to other commercial banks as well as declining to have itself governed by specified standards in regard to acceptability of bills for discount. It was, for instance, pointed out before the Indian Central Banking Enquiry Committee[165] that

> "The Imperial Bank of India is prepared to discount only approved bills *i.e.*, bills approved by it. It does not lay down any standards for the guidance of other banks as to what constitutes an approved

* The working of a modern bill of exchange is an interesting phenomenon, and it would be useful for the reader to understand at this stage how it works. See, e.g., Davar—Law and Practice of Banking, Ch. IV.

165. Report p. 409.

> bill in its opinion. The result is that joint stock banks cannot depend on bills which they discount for their customers being rediscounted by the Imperial Bank of India".

One can only wonder as to what enabled a bank, using funds of the Government of India and earning its profits from business in India, to adopt such an attitude and, what is more, get away with it. In fact, the Imperial Bank was most reluctant to adopt anything Indian, and, its Managing Governor had even the opportunity to suggest[166] that indigenous bankers must use credit documents acceptable to the commercial banks, rather than use its position and privileges to develop an existing local banking system.

12·4 *Reserve Bank's Scheme for Developing a Bill Market in India.* In 1931, four years before the Reserve Bank of India was established, the Indian Central Banking Enquiry Committee[167] had expressed the view :

> "There is little doubt that the creation of the Reserve Bank with the resultant coordination of the various elements of the money market and a unified control of credit and currency should do much to develop the use of commercial bills and ultimately create an active and efficient discount market in India. The mere fact that during the busy season the Issue department of the Bank will be enabled to issue currency freely against genuine trade bills without the Bank Rate being raised to artificial levels should have a psychological effect on merchants generally and encourage them to take advantage of a cheap and convenient form of short credit. The prestige and standing offered to indigenous bankers who decide to come within the scope of the rediscount facilities of the Reserve Bank should tend to link up the indigenous money markets with the large centres whose surplus funds tend to concentrate. There should no longer be any jealousy or feeling of uncertainty as regards the rediscount of bills by joint-stock banks with the Reserve Bank; and if, as we propose, the published rate of the Reserve Bank is its rate for the rediscount of first class trade bills, which will be its lowest operative rate, the money market as a whole should gradually come to take advantage of this rate as a natural

166. Report of the Indian Central Banking Enquiry Committee, p. 413.
167. Report, para 604.

> practice in lieu of the present crude method of taking advances against securities at a higher rate for shorter periods."

This was, more or less, a fairly detailed and self-contained suggestion. The Reserve Bank of India was established in 1935, but under the influence of a conservative banking policy it refrained from paying adequate attention to the problem of developing a bill market. All that it did was to agree to extend rediscount facilities to the indigenous bankers provided they were prepared to

(i) segregate their non-banking business,

(ii) discard non-banking business within a specified period,

(iii) maintain proper books of account, and,

(iv) get them audited and make available to the Reserve Bank for inspection.

These proposals, which were made in 1937 and, again, in 1941 were doomed to failure from the very beginning for it was like asking water to flow uphill. It was true that in the absence of a standard usance bill it was difficult for the Reserve Bank to go ahead, but instead of taking steps to standardise the *hundi* it waited, in true dignified fashion, for the *hundi* to alter itself. It was not until the country became independent and subsequently nationalised the bank that the Reserve Bank made any positive move in this matter. In January 1952, the Reserve Bank announced a scheme for the creation of a bill market. The main features of the scheme were as follows :—

(a) scheduled banks were allowed to convert a part of their loans and advances against promissory notes into usance promissory notes with 90 days' maturity so as to cover the minimum requirements of the borrower,

(b) such facility was available to scheduled banks having deposits of not less than Rs. 10 crores,

(c) a minimum limit of Rs. 25 lakhs was fixed for each advance, and

(d) a minimum limit of Rs. 1 lakh was laid down for each bill.

The scheme, however, was liberalised in June 1953 so as to include banks with a deposit of Rs. 5 crores and, in July 1954 all scheduled banks were included in the scheme. The minimum limit of each advance was reduced from Rs. 25

lakhs to Rs. 10 lakhs and the minimum for each bill from Rs. 1 lakh to Rs. 50,000. In October, 1958 the scheme was extended to include export bills as a measure of assistance to exporters. Since it was felt desirable to make the benefit available to the smaller exporters also, the minima for the amounts to be advanced to a bank at a time and for the amount of an individual usance promissory note to be accepted as security have been fixed at Rs. 2 lakhs and Rs. 0·20 lakhs, respectively, as against Rs. 5 lakhs and Rs. 0·50 lakhs fixed for the others. These relaxations have made the scheme popular and considerable use has been made of the accommodation provided under the scheme which is made available under Section 17(4) (c) of the Act.

12·4 *Appraisal of the Bill Market Scheme.* In spite of the growing popularity of the scheme, it cannot be said that it has, as yet, become a basic part of the functioning of the money-market. Further, the scheme as it operates at present can hardly be called a proper scheme for a bill market. Actually it is an attempt to convert loans and advances of scheduled banks into usance bills, rather than develop genuine trade bills. Further, it is mostly used for extending credit during the busy season, because normally the scheme is cumbersome and costly. Finally, the scheme still keeps out the *hundis* of indigenous bankers so that an important sector of domestic trade, particularly that part operating in the rural areas, has been excluded from the benefits of the scheme. It is difficult to visualise how a full-fledged bill market scheme can be developed for India unless indigenous bankers are brought into this scheme and scheduled banks are encouraged to accept their *hundis* with facilities for rediscounting them with the Reserve Bank of India.

13. Legislative Regulation of Banking.

13·1 *Need for Regulation.* The basis for all regulation of private sector activities is the need to guard against misuse and mismanagement, and to ensure conformity to national policies. The importance of banking in modern economy is sufficiently great to justify a special banking law for its regulation. Banks are custodians of the savings of the people and no Government can look upon with equanimity the misdirected activities of institutions who exercise a very powerful influence on the economic life of the country. Banking business must be regarded as quasi-public in its nature and must be subjected to a minimum degree of formal regulation and control. It is not implied that regulation by itself can ensure efficiency for it would always be true that good banking is achieved by good bankers rather than by good laws. Even then,

however, a comprehensive and special law regulating banking would be desirable in the public interest with a view to bringing about at least a minimum degree of precaution against mismanagement. Quite frankly, laws cannot prevent bank failures ; it can only ensure that they are not due to gross negligence of supervision and are not the outcome of unchecked 'shady' business.

13·2 *Origin of Banking Legislation in India.* Till 1936, India had no banking legislation as such and banks were required to conform, like any other concern, to the general requirements of Company Laws. The haphazard development of Indian joint stock banks during and after the Second World War led to many bank failures. The serious blow to depositors following from these failures led to the issuing of an Ordinance in 1946 whereby the Reserve Bank of India was empowered to inspect accounts of any joint-stock bank and to take action against any bank whose affairs were regarded as unsatisfactory and detrimental to the interests of depositors. The subsequent enactment of the Indian Banking Companies Act of 1949 marked the culmination of a trend towards increasing banking regulation.

13·3 *The Banking Companies Act of* 1949. This Act is a most comprehensive piece of banking legislation and marks an important landmark in the history of banking development in India. Theoretically, the objective of banking legislation should be

> "the protection of the public against its own ignorance, protection against the ignorance or dishonesty of those who float or manage banks and finally the protection of Indian banking generally against powerful foreign competition."[167]

The following are the main provisions of the Act :—

(1) Banks have been defined and their functions indicated exhaustively ; a prohibition has been added to the undertaking of any business other than those enumerated and trading, *i.e.*, buying and selling of goods, has been expressly disallowed ;

(2) It has been provided that non-banking assets, like immovable property, acquired because of failure to repay advances made must be disposed off within a specified time ;

(3) Companies carrying on banking must use the words 'bank' or 'banker' in its name and other companies must avoid these words in their description ;

167. Muranjan, S. K.—Modern Banking in India, p. 342.

(4) Prior licensing by the Reserve Bank of India has been made compulsory ;

(5) Minimum requirements of paid-up capital and reserves have been laid down with a view to checking the growth of banks with inadequate financial resources ;

(6) Minimum reserve requirements have been laid down to ensure liquidity of assets ;

(7) Inspection of any bank by the Reserve Bank, either on its own initiative or when directed by Central Government, has been provided ;

(8) Managing agents have been prohibited from managing banking companies;

(9) Interlocking of directorates amongst banks has been prohibited;

(10) The Act prohibits starting by banks of subsidary companies,

(11) It seeks to combat concentration of power by restricting the total votes acquirable by an individual to a maximum of 5 percent of the total voting rights of all shareholders; and

(12) Prescribes the form of the balance-sheet and makes audit compulsory.

The Act was amended a number of times during the last decade but most of these amendments were by way of clarification or rationalization. The most important amendment was undertaken on March 24, 1961 which enabled compulsory amalgamation of a banking company with State Bank of India or its subsidiaries. This was a revolutionary step forward as previously such amalgamation was possible only with another banking company. The new legislation also enables amalgamation of more than two companies by a single scheme.

14. Insurance of Bank Deposits.

14·1 Inspite of a comprehensive banking legislation providing for wide powers of control and supervision by the Reserve Bank of India, bank failures took place even in 1960, and, of a scheduled bank. This has shaken the confidence of the depositor and it was necessary to at least provide a semblance of safety to them, particularly those deposits which are of small amounts.

14·2 The Banking Companies (Second Amendment) Act, 1960 sought to facilitate expeditious payment to the depositors of banks in liquidation. It also sought to protect the interest of savings bank depositors (who are presumed to be individuals with moderate means) by laying down prior payment to every saving bank depositor the balance at his credit subject to a maximum of Rs. 250 before any other depositor is paid. The intention obviously was to make minimum payments available to depositors of moderate means.

14·3 It is now proposed to introduce a scheme of deposit insurance with a view to providing greater safety to the deposits of individuals, specially those of limited means. Under the scheme, a separate autonomous corporation will be set up with an authorised capital of Rs. 5 crores which will be allotted entirely to the Reserve Bank. The proposal is to ensure the deposits of all commercial banks functioning on the date of introduction of the scheme. The scheme would, however, exclude the deposits of the State Bank of India and its subsidiaries in view of their special position, though these State associated banks would, nevertheless, be required to contribute to the funds of the corporation. The limit of the amount of individual deposits insured and the rate of premium will be fixed by the corporation. It is provided that approval of the Central Government would be required before these are fixed and that they may be varied from time to time. Tentatively, however, the idea is to guarantee, to begin with, individual deposits to the extent of not less than Rs. 1,000. The actual figure will, of course, be determined by the corporation after it has been formed.

14·4 The scheme essentially aims at winning back confidence of the depositors which has been shaken by recent bank failures, particularly as it revealed that the much boasted inspection by the Reserve Bank of India provided no safety against unsafe banks. Bank failures, however, are not due to natural calamities but are the result of mismanagement and non-adherence to the principles of sound banking. If the failure of a particular bank creates conditions of panic and a simultaneous loss of confidence in the banking system as a whole emerges, it is doubtful whether the deposit insurance scheme would be of much value. In any case, the problem for a bank in difficulties is to obtain liquid resources in the short period, and this should not prove difficult if its temporarily frozen assets are ultimately sound investments. It would seem more proper for the Reserve Bank of India to recognise that the nation expects it to save banks rather than make payment of deposits, through its insurance, after a bank has failed. As the custodian of the banking system, the

Reserve Bank should ensure that each and every bank is a sound and viable unit ; ——it is not enough for it to take shelter behind meaningless generalisations by stating that "the Indian banking system, taken as a whole, from the point of the safety of deposits, is sound and vigorous." There is no such thing as the safety of the banking system ; there are only safe banks.

XI

A DECADE IN RETROSPECT

1. Were the "good" old days really good? Perhaps the answer lies not so much on facts, and what the statistician loosely calls figures but on one's personal economic theories. It is difficult to convince the businessman that unrestricted competition was unhealthy, not because it brought cyclical declines in his profits but because it prevented realisation of human values. Nor is it easy to persuade the administrator to recognise that the economy can get on, and get on fairly well, without his wisdom and, consequential, controls. Whatever the theory and whatever the fact, the old days—good or bad—are gone, possibly for ever; certainly, for a long time to come.

2. The decade that has just gone by represents to India a decade which brought about a change in our thinking process and is marked by the emergence of a philosophy and faith in planning. The economic theory of planning may be correct or incorrect. The claims made as to the potentialities of planned development may be supportable or not. These are matters on which endless debate is possible, but would be futile. The country has taken the plunge and adopted for itself the view that the shape of things to come is to be determined not by the traditional concept of individual preference but by directions issued by the process of planning. But we have not abandoned the free market economy. Our economic development is still hinged to a price-mechanism and we have rejected the totalitarian techniques. Our aim is to attain economic progress through induced change while retaining the essentials of democracy. We have our Fundamental Rights; but, we also adopted the Constitution (Fourth Amendment) Act, 1955, by which the right to question the amount of compensation awarded by appeal to judicial procedure in the ordinary Courts of Law has been expressly withdrawn. The withdrawal of the right to appeal to the law courts, set up by the country itself, does not necessarily mean that there is a reasonable

possibility, or even a remote one, of compensations actually paid being inadequate or unjust; but, it does indicate the denying of a right to an aggrieved party, and, reflects trends in the body-politic which may, if unchecked, create the roots of totalitarianism. It is true that the wholesome respect that India h s in the value of individual personality, coupled with centuries of a philosophy of 'toleration', would keep us from crossing the brink and falling down the precipice, but it would be wise to remember that in matters of economic regulation, controls have a habit of breading further controls until they achieve a sort of a self sustaining growth or Parkinsons Law of Expansion.

3. Planning imposes a new obligation on planners. Apart from achieving a higher rate of growth, planners must also recognise that an obligation to safeguard the interest of the individual is imposed upon them in so far as the process of planning curtails the freedom of the individual to protect his own economic interest, subject to the law, by his own preferences and choice. The same would apply to the producer. The more Government 'directs' the industry, the less is the freedom of the entrepreneaur to perform his legitimate economic functions, and, the more, logically, is the necessity for Government to perform those functions on behalf of the producer to enable realisation of the objectives laid down. In short, planning involves regulations and regulation in one sphere may often necessitate further regulation in a complementary sphere.

4. The fundamental objective before India is the raising of the levels of living by exploiting more fully the productive potential of the country. But these are to be achieved along with an adherence to the ideology of the "socialist pattern of society." Further, the large unemployed labour force compels recognition that unemployment is an evil in itself so that, as between given alternatives, the choice in particular spheres may sometimes have to be on labour-intensive, rather than capital-intensive, projects. In this sense Indian planning is concerned not only with 'ends' but also with 'means' and, the theory of neautrality for the economist as between alternative ends has no significance in India. Thus, the 'ends' before us is not merely the growth of overall national income or, or even per capita income or greater equality of incomes, but a rise in levels of living consistently with growth of overall employment, diversification in the pattern of production and employment and balanced regional growth. Logically, such a variety of 'ends' to be pursued simultaneously may involve acceptance of a lower rate of growth in any or each one of them; but, the choice has been made and it is

the enlargement of the aggregate of human happiness that is being sought and not the maximisation of national income. It is not mere material progress that India strives to achieve our traditional philosophies are contrary to such an attitude.

5. The primary indicator of economic progress is the growth of National Income* The table given below shows what progress has been achieved in this field :—

Year	INDEX of National Income at (1948-49) Constant Prices	INDEX of Per capita income at (1948-49) Constant Prices
(1)	(2)	(3)
1950—51	100	100
1951—52	102.8	101.1
1955—56	118.4	108.2
1956—57	124.3	111.4
1959—60	132.9	111.9
1960—61	141.6	116.7

To many the rather slower rate of growth of *per capita* income represents unsatisfactory achievement. Few, however realise that much of the increase in population during the decade was due to a fall in mortality rates which in itself constitutes a great achievement. Thus, while it is true that a large part of the increased national income was absorbed by the increase of population, so that only a portion was available for raising per capita levels of income, that by itself is no cause for disappointment, for judged by human values in the decline in mortality rates and increase in average expectation of life there has been a degree of achievement for which the country can be justly proud†.

6. A low *per capita* income must necessarily mean a low level of consumer expenditure ; and, India is no exception to this general rule. Estimates of our per capita consumer expenditure are not without their own limitations, but even allowing for shortcomings of data, one is forced to the conclusion that in certain categories of income, the level of consumption expenditure has been below the minimum desirable sustenance standard, ‡ and, has remained so in spite of a decade of planning.

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* For details, see Vol I, pp. 158—60.

† See Vol I, pp. 84—91.

‡ See Vol I, pp. 6—7.

7. The relative growth of the different sectors is a matter of deep concern in a planned economy. Agriculture gave some ground to non-agricultural pursuits in the national economy for its percentage contribution to National income fell from 51·3 in 1950-51 to 48·3 in 1960-61. The contribution of mining and industry rose during the same period from 16·1 to 18·6[168]. Agriculture, however, continues to be the dominating factor in Indian economic life, with a good harvest as still the basic factor in setting the tempo of economic activity during a year. Judged by the index of agricultural production, the rise during the decade was about 40 percent, giving a fairly satisfactory average annual compound rate of growth. The real progress, however, was much more fundamental for considerable preparations for sustained agricultural production were undertaken through large irrigation projects which are yet to bear fruit. Not only did the area under irrigation increase substantially (by almost 35 percent) during the decade, there was also an increasing recognition given to the value of fertilizers and improved seeds, whose consumption increased sharply. These are expected to bear fruit in the Third Plan Period during which agricultural production is expected to rise by another 30 percent. The rise of industrial production was most impressive and the index of industrial production rose by more than 80 percent during the decade. It is well-known that the present index of industrial production does not take into account all new industries established during the last decade, so that, in effect, the achievement in the field of industries leaves little reason for dissatisfaction, especially as regards heavy, chemical and engineering industries. Employment in the industrial sector increased substantially, though in spite of this rapid rise, overall visible and invisible unemployment continued to be high.*

8. The essence of modern planning is to step up the rate of investment. Unfortunately, statistical data relating to investment are sadly incomplete, and, even where available, unsatisfactory. It was not till 1961 that the Central Statistical Organisation provided some estimates of capital formations, prior to which only the investment estimates given by the Planning Commission were available. There is a lack of agreement between the two estimates, which is indicated as follows :—

168. See National Income Estimates released by C.S.O.—table 2·1; also Vol I, p. 161.

* See Vol. I, relevant portions, particularly pages 181-84, 231-33 and 95-107,

Percent of Net Investment in	Planning Commission estimate	C. S. O. estimate
(1)	(2)	(3)
First Plan	7	8
Second Plan	11	13

Despite the differences in the figures (explainable perhaps by methods of estimation there has been a marked increase of investment. The rate of gross investment is estimated to have risen from 13·6 percent of gross national product in the first plan to 18·5 percent in the second plan, which, even after allowing for statistical errors, is something of which the country can justly take credit for it was no small achievement.

9. The decade showed a remarkable achievement in the development of power. The index of electricity generated showed steady and substantial growth. In fact, its rise was phenomenal, the index (Base 1950-51=100) rising from 114·3 in 1951-52 to 163·9 in 1955-56 and achieving 301·9 in 1960-61.* It is true that the rise is somewhat illusory because of the low availability in the base year, but even than, per capita availability was more than doubled during the decade, though it is still low compared to the more advanced countries. However, the major lines of improvement in this respect seem to be the necessity of more extensive rural electrification and making available power to small scale industries.

10. In view of India's size, the importance of a well-planned system of transport and communication is very great. A big slice of public investment was made available for transport, though towards the end of the decade there were signs of shortage indicating both excessive strain and bottlenecks. There is a feeling in certain quarters that the percentage alloction on transport for the third plan should have been higher.[169] It must be admitted that investment in transport is a crucial necessity in an era of planned development, but allocation, when total resources are limited, is ultimately a question of priorities and it is easier to say that investment in a particular sector should be increased but more difficult to indicate from where it should be cut. Considering, however, that expenditure on social service in India was one of the lowest in the region,[170] it is difficult to seriously suggest

* See Vol. I, p 58.

169. L. A. Natesan, article in Problems in the Third Plan p. 164.

170. U. N.—Economic Survey of Asia and the Far East, 1960, p. 78.

that transport investment should have been increased by diverting funds from social services, and, it would obviously have been unscientific to have cut down investment in basic production lines, for transport is intended to serve increases in trade and not become an end in itself.

11. The rate of domestic savings has been both low and discouraging. The third five year plan is based on expectations of its increase, but the realisation of the expectation seems doubtful.* The failure of the rate of domestic savings to rise has been primarily due to an increase in propensity to consume, particularly in the rural sector. Such an increase in consumption expenditure, however, was inevitable because of the low level of living which exists, and where every increase in disposable income must mean more consumer expenditure to achieve a higher standard of living. Nor is all additional consumption expenditure a matter of regret, since much of it may be investment in 'human resources' in the form of better education, better health condition and better nutrition.

12. The most troublesome feature of the decade was the widening gap between India's foreign income and spending of foreign exchange. Part of the widening gap was due to sharp increases in imports, most of which was unavoidable, but mainly it was a consequence of the inability of exports to rise. While no precise correlation between exports and national product should be sought, it would seem that for a country seeking to step up exports, it should tend to become a larger percentage of national product. Actually exports, which were 5·8 percent of national product in 1950-51, fell to nearly 4·3 percent in 1960-61. Since the trend of export-prices of our goods cannot be assumed to be always rising to our favour, the gap in our balance of payments has to be met more and more by quantitative expansion of our exports rather than by a favourable movement of terms of trade. It has been possible for the country to carry through its development effort without any significant curtailment of plan ceilings mainly because it was possible to "eat" into our foreign balances which were large in 1950-51, thanks to the enormous acquisition of sterling assets during and after the Second World War. Further, considerable "aid" from foreign countries‡ enabled us to tide over the period fairly smoothly. There has, however, been an enormous increase in our foreign liabilities as a large portion of the "aid" was

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* See Vol. I, pp 489-90.

‡ See Vol I. Ch XII.

received as loans. Thus, there has been a sharp increase in foreign indebtedness and a considerable running down of our foreign assets, so that a situation is rapidly emerging which cannot but cause considerable worry.

13. The strategy of Indian planning was to prefer a capital-intensive approach for economic growth. The emphasis was on heavy industries* and industries that would aid the growth of consumer goods industries. In the particular context of a shortage of internal physical resources of the required nature, it imposed on the country an import-intensive approach, which involved considerable inroads on our accumulated foreign assets. The policy was intended to speed up the pace of growth. It is possible that the rate of income growth have been small in terms of investment because much of the latter was obtained at high prices. It is also equally possible that rapid technological advances all the world over may lead to our export industries becoming comparatively inefficient because of obsolescence of our fixed capital making realisation of an export surplus more and more difficult. But planning in India could hardly have taken any other course, for rapid industrialization was the only choice that could have satisfied the country's hunger for development.†

14. Government draft on private income increased during the decade, as it was naturally expected to, but it is doubtful whether the rate of increase was either sufficiently fast and adequate, or whether the distribution of whatever increase that took place was in accordance with the fundamentals of ability to pay so as to make it more equitable. The table given below provides interesting information :—

Government Draft on Private income.
Percent of private income

Item	1950-51	1955-56	1959-60	1960-61
(1)	(2)	(3)	(4)	(5)
1. Direct taxes	2·4	2·6	2·8	2·6
2. Indirect taxes	4·5	5·5	6·9	6·8
3. Miscellaneous fees, etc,	1·1	1·4	1·5	1·4
Total	8·0	9·5	11·2	10·8

Source : C.S.O. National Income Estimates.

* See Vol. I, pp. 252-53.
† See Vol. I, p. 222.

The slight setback in 1960-61 was perhaps only 'statistical' as the National Income Estimates for 1960-61 underwent upward revisions due, *inter alia*, "to the incorporation, for the first time, of the results of random crop cutting surveys in respect of rice in Orissa and maize in Bihar." This changed use of source material (for which no adequate justification has been given) led to a statistical (and illusory) increase in National Income. It has been admitted[171] that

> "If correction is made for such statistical changes, the overall increase in the total national income and in the *per capita* income during the Second Plan period would work out at about 20·2 p.c. and 8·4 p.c. respectively (without applying the correction the figure would be 21·1 p.c. and 9·2 p.c. respectively)."

Since no clarification has been given in the White Paper as to why the change was adopted, it is difficult to assess its validity or otherwise ; but, it does appear rather strange that in the last year of the Second Plan period a change in the source of statistical data should have been adopted which would make the latest figure of estimates (of an important item like foodgrains) not strictly comparable with those for the earlier years of the Second Plan.

However, even if allowance is made for the "fictitious" increase in National Income in 1960-61, the Government's draft on private income failed to increase adequately during the Second Plan period. Even tax-revenue as such perhaps did not increase as steeply as was desirable.* There were undoubtedly good reasons for the financial policy followed, though the inescapable necessity of having to place increasing reliance on indirect taxation was a feature that requires careful understanding.

15. Apart from taxation and non-tax revenues, the decade is marked by a large increase in net market borrowings by the Central and State Governments. It is elementary knowledge that Public Revenues are non-repayable transfers from the income of the people to the Public Exchequer while State borrowing, being repayable, is only a temporary transfer of resources from the hands of the public to that of Government. However, during any given period, the total of the two constitutes the sum total of resources which, instead of being available for spending by private initiative, becomes

171. C.S.O.—White Paper on National Income, February, 1962, —See. Notes, para 9.

* See Vol. I, p. 272; for detailed discussion of the problem refer to Vol. I, Ch. VII, and Ch X.

available to the Government for undertaking public expenditure. Of course, all such transfers are not necessarily from current income. One could, for example, undertake consumption expenditure from past savings (thereby paying some indirect taxes) and not from current income. Similarly a part of current subscriptions to Government loans floated may be by conversion of other investments. Thus, so far as market borrowings by governments are concerned, it is the net absorption by the public rather than gross floatation in any given year that is important. The net absorption of Government securities by the public is equal to

(a) Cash subscriptions of the public — (b) Cash repayments to the public of maturing loans

+

net open market

(c) Sales by the Reserve Bank

+

Sales by the

(d) Government operating through cash balance investment account.

The place of loans in public finance, particularly the role that governmental borrowing should play in a planned developing economy, raise issues which are complex and controversial. But leaving aside for the time being considerations of theory relating to public borrowing[172], it would be useful to get a clear idea as to the net absorption of government securities by the public so as to dispel the common misconception that large floatation of public loans mean equally large immobilisation of resources from the hands of the public.

For a proper understanding of the table, on the next page it is necessary to bear in mind that the figures of net absorption of Government securities by the public since 1956-57 has been influenced by the investment or disinvestment of P.L. 480 funds, and the change in the procedure of accounting introduced in May 1960 affected the figure for 1960-61 and 1961-62. From the table given it would appear that there was in fact a net *disinvestment* of Rs. 64 crores approximately in 1960-61, which was in great contrast to the net absorption in

172: See Pigou, A.C.—A study in Public Finance, Pt. III, Ch. I

NET Absorption of Government Securities by the Public

(Crores of Rs.)

Period	Net market borrowing by the Central and state Governments: Cash Receipts	Cash Payments	Net Receipts (2 - 3)	Net cash receipts from the public	Open Market purchases (—) from / sales(+) to the public	Net absorption by the public (5+6)e
(1)	(2)	(3)	(4)	(5)	(6)	(7)
1. First Plan total (1951-52 to 1955-56)	359·8	182·6	+177·2	+192·3	+ 97·6	+289·9
2. Second Plan total (1955-56 to 1960-61)	872·7	125·8	+746·9	+367·3	+ 90·6	+457·9
2A. 1960-61	179·4	45·4	+134·0	+ 61·4	—125·1	— 63·7
3. Third Plan 1961-62	185·7	50·0	+135·7	+ 73·0	— 37·0	+ 36·0

Source : R. B. I.

each of the previous four years. The detailed year-wise figures bring out the position more clearly :—

(crores of Rupees)

Year (Second Plan Period)	Net absorption (+or—) by the public
1956-57	+ 70·6
1957-58	+113·3
1958-59	+194·6
1959-60	+143·1
1960-61	— 63·7
Total	+457·9

Source : R.B.I.

However, the net investment or disinvestment can only be calculated if allowance is made for the operations of P.L. 480 deposits and the manner of their investment in Government securities. This is rather a technical operation, but briefly (and shorn of technicalities) the position is as follows : —

(a) Prior to May 1960, these funds were being deposited by the U.S. Government with the State Bank of India, who invested them in Government securities, though it is known that a part of these funds were utilised by the State Bank for investment in Treasury bills and also for extension of credit to the private sector in the initial stages of the accrual of these funds to the State Bank,

(b) Since May 1960, these funds are flowing directly to the Reserve Bank which invests them in special Government securities,

(c) Part of the accumulations made in the past of the P.L. 480 deposits with the State Bank was transferred during the period July 1960 — June 1961 in monthly instalments of Rs. 12 crores each leading to a disinvestment of securities by the State Bank of India.

To arrive at the figure of net absorption of Government securities by the public, it is necessary, therefore, to eliminate the special factor of P.L. 480 funds. Allowing for such elimination would really mean that figure of net absorption for the Second Plan period as a whole would be less than given above and the annual figures would also show variations. Allowing for this, the net absorption (ignoring the small effects of (a) above) of Government securities by the public,

> "during 1960-61 would amount to Rs. 53 crores and for the Second Plan period as a whole to Rs. 257 crores or an average of Rs. 51 crores a year as compared to Rs. 290 crores or Rs. 58 crores a year for the First Five Year Plan (1951-56)"[173].

The decline in net absorption in the Second Plan period over that of the First Plan period is a matter which needs careful consideration for it is obvious that the aggregate figures gave an illusory index of greater absorption which was misleading for it was, in effect, brought about by the operations of P.L. 480 funds rather than by net increases in domestic saving.

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173. See Reserve Bank of India Bulletin, April 1962; also see p. 274 earlier.

16. In the field of financial relationship between the Union Government and the State Governments, the Report of the Third Finance Commission, 1961, marked an important step forward in the recognition of the role of tax-division as a method of combating regional imbalance in economic ability. The Second Finance Commission (1956) had inaugurated an era of 'population' worship, for in its scheme of division of resources for the two major taxes—Income tax and Excise Duties—it had made 'population' as the chief basis for benefits.* The Third Finance Commission broke new ground by recognising that for the distribution of the proceeds of the Union Excise Duties (which was the chief and growing form of indirect taxation in the country), "The relative financial weaknesses of the States, the disparity in the levels of development reached, the percentage of scheduled castes and tribes and backward classes in their population, etc. should be taken into account in determining the share to be allocated to each State individually. In other words, we feel that in this permissive participation, an attempt should be made to bring all the States, as far as possible, to a comparable level of financial balance."[174]

Basically, it involved the idea of using tax division as a means to transfer resources from the people of one State to those of another *via* the Central Government, and, thereby, recognising that redistribution of economic resources extracted by taxation could legitimately further the objective of promoting financial balance. In the field of income-tax distribution also, the Third Finance Commission[175] recognised that population was an inadequate norm for measuring the extent and cost of rendering administrative and social services, and, emphasised the need for linking 'Collections' with the maintenance of economic and social conditions necessary to bring those large collections into existence. Union-State financial relations in India has during the past decade been governed by rather mechanical approaches based on concept of needs (measured by population) and balanced budgets† with the unfortunate result that a powerful weapon was not used to further the objective of removing regional imbalance. A departure has been made and it should now be possible to make increasing use of the device of discriminatory and differential shares in tax revenues of shared taxes to further the objective of transferring resources from the high income States to low income States to promote economic growth.

* See Vol. I, pp. 368-71, 375-78.

174. Report, of the Third Finance Commission (1961) para 47.

175. Report para 35.

† See Vol. I, Ch. VIII.

17. Central planning, in a federal constitution, necessarily involves risks of curtailment of the autonomy of the constituent States.* In fact, "there is a general feeling that the contents of the autonomy of the States are being diluted not only by the prescription of detailed directions on subjects within the State List, but also by unilateral financial decisions taken."[176] Even if in reality no significant curtailment of autonomy of the States were actually taking place, the existence of such a feeling is likely to prevent the fullest utilisation of the country's potentialities for economic progress. Further, such a feeling, coupled with financial dependence, must necessarily bring about demoralisation, which can do no good to a country engaged in the gigantic task of raising the level of living of 438 millions of people. A proper balance between conflicting claims of dual loyalty inherent in a federal constitution has to be achieved and we must appreciate that while in "a planned economy a measure of centralisation and even regimentation is inescapable, it is no less necessary that States should not feel that their autonomy is being unduly frustrated."[177]

18. Whatever may be the philosophy behind central control *versus* regional antonomy, one thing is certain, *viz*, that many of the big projects in the State sector would not have been possible without Central aid—by way of loans and grants. The decade marked the growth of a large number of big and expensive projects—in the field of power and in the field of irrigation, or, through multipurpose projects—in the various States with the assistence of Central Government. The benefits of these projects are not always measurable by a calculation of direct returns and repayment obligations, for by far the greater advantages have been reaped indirectly through benefits which are partly immeasurable, mostly general and operating to the advancement of the economy as a whole. It would, for instance, be unwise to measure the benefits of an irrigation scheme merely by the yield from the bettement levy and the increase in land revenue, or even by the increased production of agricultural goods. These are only the primary benefits. The larger benefits may come from the greater sense of security that it gives, from the reduction in the fatalistic attitude to life that must come about, from the decline in variability of income of the cultivator from year to year that emerges from greater stability--all these and many others, most of which are immeasurable in economic terms. Similarly, unutilised power generated is certainly a

* See Vol. I; p. 20.
176. Report of the Third Finance Commission, 1961: para 85.
177. Report of the Third Finance Commission, 1961, para 66.

loss, but a loss which may be worth many times its value because of the development of personality that it may bring about in those few isolated villages which have had the good fortune to be a part of rural electrification. Not that there has been any waste of power generated in India through under-utilisation ; in fact, there are severe shortages ; but, it seems necessary to emphasise that the value to the nation of a given investment does not lie in a narrow calculation of a financial balance sheet but must be evalued through a wider approach of overall values of human happiness. The statistician in India has undoubtedly done a good job by calculations of capital output ratios. It is, however, necessary to bear in mind that the sum total of human happiness is not a statistical concept. A good plan must recognize both 'the visible and the invisible dimensions' of achievement. It is time India realised that the statistician can deal only with the 'visible'; but, by far the more significant part of the achievement may lie in the 'invisible'. What we need is not so much statistical appraisal and statistical indices, nor a series of ratios and equations but an evaluation of the sum total of effects. As the Second Five Year Plan[178] rightly stated :

> "The need for evaluation exists in all fields of development and more especially in those in which new or expanded activities are being undertaken. In all planned development many unknown factors have to be reckoned with. Understanding of the interaction of different elements that enter into programmes which bear closely on the life of the people can be of material help in enhancing their contribution to the welfare of the community. Evaluation has, therefore, to be increasingly orientated towards studies of a selective and intensive type, motivated by and leading to purposive action."

And, in this great task of evaluation, the statistician has only a subordinate role, for statistics should be used for illumination and not for support. In India, unfortunately, statistics are far too often used as a drunken man uses a lamp-post—more for support than for illumination !*

19. The decade was marked by a switch of emphasis from single purpose projects to what are known as multipurpose projects, combining various facilities in an integrated development programme. In the field of multipurpose projects the

178. p. 251.

* The analogy has been borrowed from a review by M. R. Bonavia in the Sunday Standard, July 1, 1962; the application of it is by the author.

limitations of statistical appraisal are most obvious for many of the benefits are hardly capable of being reduced to a set of figures. The benefits of these multipurpose projects are not confined to their direct results but extend to many indirect and secondary effects which combine together to affect the tempo of development and increase aggregate socio-economic welfare. The more important of these projects are :—

I. The Bhakra-Nangal Projects : This is intended to benefit Punjab and Rajasthan and consists of the following constructions :

(a) the Bhakra Dam across the river Sutlej,

(b) The Nangal Dam at a point about 8 miles down stream.

(c) the Nangal hydel channel,

(d) the Nangal power house,

(e) the Bhakra canal system, and

(f) power houses at Kotla and Ganguwal

Even though the project was started in 1946, it has not yet been fully completed, though the only remaining portions relating to the Bhakra Dam and its power houses are in their final stages. The total cost of the project would probably exceed Rs. 171 crores, and, it is expected to provide irrigation facilities to 3·6 million acres of land and have a total installed capacity of 594,000 kw.

II. The Damodar Valley Project. This is intended to benefit Bihar and West-Bengal by securing unified development of the Damodar and Borakar River Valley. The constituents of the project are :

(a) multipurpose storage dams at Tilaiya, Konar, Maithon and Panchet Hill with attached hydro-electric stations,

(b) a thermal power plant at Bokaro, with an estimated capacity of 225,000 kw.

(c) a power-transmission grid covering more than 800 miles,

(d) a barrage at Durgapur with

(i) irrigation channels,

(ii) a navigation canal,

The Damodar Valley Project is a multipurpose project *per se* for it combines in itself all the four objectives of

(i) flood control,

(ii) irrigation,

(iii) electricity generation,

(iv) all the year round navigation.

The project was organised on the lines of the Tennessee Valley Authority of U.S.A. and the Damodar Valley Corporation was set up with considerable decentralised authority. The D.V.C. has already spent nearly Rs. 150 crores and the Third Plan estimates provide for an expenditure of another Rs. 80 crores approximately. The following portions of the work have so far been achieved :

(1) The Dam and Power house at Tilaiya have been completed, and, the Bokaro Thermal Station has started functioning,

(2) Konar Dam has been completed ; this is intended for supplying cooling water to the thermal power station at Bokaro and for controlling floods,

(3) Maithon Dam and the hydro-electric installation on the river Borakar has been completed,

(4) The Panchet Hill Dam and hydro-electric installation on the river Damodar have been undertaken and the hydel station at Panchet has come into operation,

(5) The Durgapur Thermal Power Station and the Bokaro 4th Unit have been completed,

(6) The Durgapur Barrage has been completed and the navigation system which will join the Hooghly 35 miles above Calcutta is expected to be completed during 1962.

III. The Hirakud Dam Project. This is expected to assist in the upliftment of Orissa and consists of what is claimed to be the longest earth dam in the world with the biggest water reservoir in the country. It was inaugurated in 1957. Like the D.V.C., it seeks to combine

(i) flood control by reducing flood danger to nearly 8,000 sq. miles of Orissa, particularly in the Cuttack and Puri districts,

(ii) provision of power by generating a commissioned installed capacity of 123000 kw by the end of the Second Plan period and a total installed capacity of 147000 kw by the end of the Third Five Year Plan,

(iii) facilities for irrigation to a gross area of nearly 1337000 acres by the end of the Third Plan and 2158000 acres on completion, having already provided 710000 acres by the end of the Second Plan.

Apart from the schemes already in operation or nearing completion, large provision has been made in the Third Plan for irrigation and flood control schemes amounting to Rs. 661 crores. This includes Rs. 436 crores for irrigation projects carried over from the Second Plan, Rs. 164 crores for new projects and Rs. 61 crores for flood control, drainage and anti-waterlogging and anti-sea-erosion schemes. Amongst the more important of the schemes* scheduled to be continued and taken up during the Third Plan period, mention may be made of the following :—

(1) Kosi Project in Bihar,
(2) Nagarjunasagar Project in Andhra.
(3) Chambal Project in Madhya Pradesh and Rajasthan,
(4) Rihand Project in U.P.,
(5) Koyna Project in Maharashtra,
(6) Narmada (Broach) Project in Gujerat,
(7) Gandak Project in U.P. and Bihar, and,
(8) Beas Project in Punjab and Rajasthan.

These projects have involved large investment of funds and adverse comments have sometimes been made as regards the deterioration in the net receipts from such projects. To the extent that appropriate financial returns are not obtained, improvements are obviously necessary and steps should be taken to increase revenues by levying adequate water-rates, imposing betterment levy and flood cess and even raising the rates of land revenue.† However, for evaluation of benefits it should be emphasised that :

> "While the financial return of an irrigation project is an important consideration, it does not by itself provide an adequate criterion for assessing the overall benefits of the project. Evaluation studies suggest that while several of the indirect benefits of irrigation cannot be assessed in precise quantitative terms, among the principal benefits to be taken into account, apart from the financial returns to Government, are more extensive utilisation of land and other resources ; adoption of a better cropping pattern and a shift to more valuable crops ; creation of conditions favourable to fresh investment or an increase in productive investment in farm business ; increase in farm productivity and stabilisation or enhancement of farm incomes ; increased employment opportunities for labour ; stimulas to industry, especially processing industries, and to trade and transport."[179]

* For details See Third Five Year Plan, p. 413—415.

† See Vol. I. Ch. X.

179. Third Five Year Plan, p. 380.

These are important and basic considerations. They are aspects of national benefit that cannot be ignored. However, a statistical recital of progress can hardly do justice to these fundamental considerations.

20. A good plan is not merely a recital of all the things that one wishes to do but must have a proper sense of priorities and provide for a strategy for economic advance. In other words, even many of the basic ideals may have to be postponed and their realisation delayed, and, compromises accepted and continued in the interests of overall progress Thus there is a dilemma in planning that creates in the short period situations that appear paradoxical. In India, for instance, we are wedded to the idea of a socialistic pattern of society, and yet it was necessary to appoint a committee to report on where all the increased wealth has gone.* In an age of commercialization and mechanised farming, we have in India laws relating to ceilings on land holdings. We recognise that taxation should increasingly be made more equitable but in practice we are compelled to raise more and more revenues through indirect taxes. Everyday the private sector has to be exhorted to play an increasing part in stimulating development, but at the same time the public sector has to be continuously extended and schemes of nationalisation increasingly given effect to. Such paradoxes and contradictions are inevitable in planning, particularly in a 'mixed' system under democracy. As the Prime Minister[180] put it :

> "The question is often asked : you talk about socialism and yet you permit grave inequalities of income ; you want to put a ceiling on land holdings and yet you oppose ceiling on urban or other incomes. There is that contradiction, of course. But if we try to remove that type of contradiction, we put a stop in many ways to the type of progress we are aiming at. If you are not prepared to change completely the whole basis of society, you have to leave enough incentive for people to work. You can, by taxation, etc. reduce disparities. But enforcing ceiling on urban incomes may well result in a slowing down of the process of development and it is of the utmost importance that this process of development and production should not come down. After all, production comes first, before any kind of equalisation or division. There is no point in having an equal measure of poverty for all."

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* The Mahalonobis Committee, whose report is still awaited; See Vol. I, pp. 4-5.

180. Speech in Lok Sabha, August 22, 1960.

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ERRATA

P. 1. Seventh line, read "indomitable" instead of "indomi-table".

P. 5. Sixth line, read "distinct" instead of "district".

P. 23. Para 6·10 first line, read "teachers" instead of "teahers".

P. 23. Fifth line from bottom, read "training" instead of "trainnig".

P. 26. First line, read "people" instead of "pepole".

P. 47. Nineteenth line, read "contribute" instead of "contril-bute".

P. 57. Table for 2·1, read "During" instead of "Durnig".

P. 70. Twenty-seventh line, read "too" instead of "to".

P. 89. Footnote, read "Review" instead of "Reivew".

P. 96. Twentythird line, read "economic" instead of "conomic".

P. 224. Last line, read "investment" instead of "investemnt".

P. 292. Twentyfourth line, read "admittedly" instead of "admitted by".

P. 329. Thirtyfifth line, read "humility" instead of "humiei-ty".

P. 351. Footnote, read "exceed" instead of "excceed".

P. 363. Fourth line, read "banking" instead of "baninkg".

P. 384. Sixteenth line, read "should" instead of "shold".

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